

THE SMALL BUSINESS MOTOR FUEL MARKETER PRESERVATION ACT

HEARING BEFORE THE COMMITTEE ON THE JUDICIARY UNITED STATES SENATE NINETY-EIGHTH CONGRESS

SECOND SESSION

ON

S. 40

A BILL TO REQUIRE THE DIVORCEMENT OF MOTOR FUEL SERVICE STATIONS FROM OPERATION BY CERTAIN PRODUCERS AND REFINERS OF MOTOR FUELS, AND FOR OTHER PURPOSES

MARCH 14, 1984

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THE SMALL BUSINESS MOTOR FUEL MARKETER PRESERVATION ACT—S. 40

WEDNESDAY, MARCH 14, 1984

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 9 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Charles McC. Mathias, Jr. (acting chairman) presiding.

Also present: Senators Metzenbaum and Biden.

OPENING STATEMENT OF SENATOR HOWARD M. METZENBAUM

Senator METZENBAUM. The committee will come to order.

Senator Mathias will be along very briefly. There was a conflict in scheduling this morning, and I have a witness coming up before another committee that I must interrogate. It is an accepted fact that I support this legislative proposal and would like to be here, but I thought it was more important to go forward with the hearing than to worry about whether I was here or not.

So I am going to excuse myself, but that is not to indicate any lack of enthusiasm or support for this legislative proposal, and I will ask the chairman, as soon as he arrives, to put my opening statement into the record, and on my behalf, to ask a few questions.

But I wanted to explain to this group that my failure to be here is not to be interpreted as any lack of enthusiasm, but rather to prove positively that I am not a split personality, and I cannot be two places at the same time.

[Pause.]

OPENING STATEMENT OF SENATOR CHARLES McC. MATHIAS, JR.

Senator MATHIAS. The committee will come to order.

We are here to hear testimony today on S. 40, a bill to require major oil refiners to divorce themselves from controlling or operating retail service stations. S. 40 was proposed in response to concern about the reduction in the number of independent gasoline dealers in recent years. It is based on a belief that the reduction is in part caused by discriminatory and anticompetitive marketing practices on the part of refiners who own and run service stations that compete with independents.

We look forward to bringing the record up to date and studying any new information that has developed since the hearing on the predecessor bill, which was held in the previous Congress.

Due to constraints on our time, oral statements will be limited to 5 minutes. The written statements will be included in full in the record.

The record will remain open for 1 month in order to provide an opportunity for the submission of additional statements and material.

I have to advise witnesses that I will be constrained to enforce the time rule very severely because of competing engagements. If I do not do that, the Sergeant at Arms may roll in a wrecker and haul me away before the meeting is over. So it is in your interest as well as mine.

At this point, I will introduce in the record a statement on the part of the distinguished Senator from Ohio, Mr. Metzenbaum, along with the text of S. 40.

[The following was received for the record:]

PREPARED STATEMENT OF SENATOR HOWARD M. METZENBAUM

Two years ago, this committee reported out legislation to protect independent service stations from the predatory and anticompetitive actions of the major oil companies. Unfortunately, that legislation did not become law.

Had we been able at that time to foresee the recent wave of massive oil company mergers, the growing concentration of power and the anticompetitive behavior by major companies against the neighborhood gas stations, perhaps we could have moved that bill into law.

In the last Congress, this bill covered sixteen oil companies. Now, two of those companies are buying two of the others. And almost every week, there are rumors of further mergers.

Today, I am sure that we will hear many of the same stories we heard two years ago.

Two years ago, we heard from neighborhood dealers who have gone under because their suppliers had jacked up rents—in some cases several times in a single year.

We heard about abrupt changes by major oil companies in credit terms.

We heard of major oil companies requiring stations to stay open 24 hours a day, even during shortages.

And we heard two years ago about how effectively the oil giants had used their vast financial power to eliminate small neighborhood gas stations—approximately 30,000 independent dealers went out of business between 1972 and 1979. And attrition continues at a rate between 5 and 10 percent per year.

These small, independent businesses are the backbone of our gasoline marketing system.

They keep markets competitive.

They create jobs and provide services to their neighborhoods. And these small businesses represent the livelihoods and in many cases, the life's savings of thousands upon thousands of hard working men and women.

I believe, Mr. Chairman, that we have a clear choice. Either we act now to provide the independent gasoline dealers with a fair opportunity to compete in the retail market, or we sit by and watch while the remaining independent gas stations are forced out of business.

The bill before this committee takes a moderate approach. It does not strip major oil companies of their right to own retail outlets. It simply precludes them from operating the outlets directly in competition with the independents. This provision is designed to take away from the majors any incentive to drive their independent dealers out of business.

The bill also increases competition on the wholesale level. Under this legislation, suppliers could no longer require dealers to sell only branded gas through existing pumps. That will leave dealers free to take advantage of free market competition in purchasing gasoline and to sell that gas through properly labeled pumps at the station.

This means that consumers could choose between branded and unbranded gas at a single gas station, just as they now can choose between name brand and cheaper store brand products at the grocery store. For cost conscious consumers, the savings from this provision alone could be substantial.

I hope that the committee will once again act favorably on this legislation. The independent gas station operators are more threatened now than ever before and with merger mania rampant among the big oil companies, it is more important than ever before that we move to protect competition in the retail gas market. I hope the full committee will have an opportunity to vote on this legislation in the very near future and I urge my colleagues to support it.

S. 40

To require the divorcement of motor fuel service stations from operation by certain producers and refiners of motor fuels, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JANUARY 26 (legislative day, JANUARY 25), 1983

Mr. METZENBAUM (for himself and Mr. THURMOND) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

A BILL

To require the divorcement of motor fuel service stations from operation by certain producers and refiners of motor fuels, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

SHORT TITLE

SECTION 1. This Act may be cited as the “Small Business Motor Fuel Marketer Preservation Act”.

6 DIVORCEMENT OF MOTOR FUEL SERVICE STATIONS; LIM-
7 TATION ON RETAIL SALES OF MOTOR FUEL BY RE-
8 FINERS

9 SEC. 2. (a) Notwithstanding any other provision of law,
10 it shall be unlawful for any refiner, other than an independent

1 refiner or small refiner, to operate any motor fuel service
2 station in the United States.

3 (b)(1)(A) Notwithstanding any other provision of law, it
4 shall be unlawful for any person to restrain, interfere with, or
5 in any way prevent the purchasing from another, the storing,
6 or the selling of motor fuel by any dealer.

7 (B) Subparagraph (A) shall not apply with respect to
8 any provision of any contract or agreement to the extent that
9 the provision requires the purchasing of any motor fuel by
10 any dealer exclusively from any refiner or distributor, but
11 only if such provision provides that such dealer may purchase
12 such motor fuel from any other person if such motor fuel is
13 not readily available from such refiner or distributor upon
14 terms and conditions reasonably comparable to those availa-
15 ble to the dealer from such other person.

16 (2) Notwithstanding any other provision of law, it shall
17 be unlawful for any dealer, at a motor fuel service station
18 displaying a trademark, trade name, service mark, or other
19 identifying symbol or name owned by a refiner, to sell motor
20 fuel which is not provided by such refiner without providing
21 reasonable notice at the point of sale to each purchaser of
22 such motor fuel that such motor fuel is not refined by such
23 refiner.

1 (c)(1) Not later than ninety days after the date of the
2 enactment of this Act, and annually thereafter, each refiner
3 shall provide in writing to the Federal Trade Commission—

4 (A) the number of barrels of crude oil produced
5 during the preceding calendar year by the refiner, and

6 (B) the number of barrels of crude oil refined
7 during the preceding calendar year by the refiner.

8 (2) Not later than ninety days after the date of the en-
9 actment of this Act each refiner shall provide in writing to
10 the Federal Trade Commission the information described in
11 paragraph (1) with respect to calendar year 1978.

12 (3) The Federal Trade Commission shall not require
13 from any person information referred to in the preceding pro-
14 visions of this subsection to the extent that the Commission is
15 able to obtain such information from agencies or departments
16 of the United States.

17 (d) For purposes of this section:

18 (1)(A) The term "producer" means any person
19 who is engaged in the production of crude oil or who
20 owns crude oil when it is produced.

21 (B) Such term includes any related person with
22 respect to such person.

23 (2)(A) The term "refiner" means—

24 (i) any person engaged in the refining of
25 motor fuel, and

1 (ii) any producer for whom refining of crude
2 oil produced by such producer, or owned by such
3 producer when such crude oil is produced, is per-
4 formed under contract.

5 (B) Such term includes, when used in connection
6 with any person described in clause (i) or (ii) of subpar-
7 agraph (A), any related person with respect to such
8 person.

9 (3) The term "independent refiner" means a refin-
10 er who obtained, directly or indirectly, in calendar year
11 1978, more than 70 per centum of the refiner's refin-
12 ery input of domestic and imported crude oil from pro-
13 ducers who are not related persons referred to in para-
14 graph (2)(B).

15 (4) The term "small refiner" means a refiner
16 whose total refinery capacity does not exceed one hun-
17 dred and seventy-five thousand barrels per day.

18 (5) The term "supplier" means any person who
19 sells motor fuel to motor fuel service stations or other
20 independent wholesale purchasers.

21 (6) The term "independent wholesale purchaser"
22 means any purchaser of motor fuel who sells the motor
23 fuel at retail or distributes the motor fuel for sale at
24 retail, but does not include any purchaser related to
25 the person selling the motor fuel to the purchaser.

1 (7) The term "related person" means, with re-
2 spect to any other person—

3 (A) a person who holds a significant owner-
4 ship interest in such other person;

5 (B) a person in whom such other person
6 holds a significant ownership interest; and

7 (C) a person in whom a third person holds a
8 significant ownership interest while holding a sig-
9 nificant ownership interest in such other person.

10 (8) The term "significant ownership interest"
11 means—

12 (A) with respect to any corporation, the
13 single largest share in value of the outstanding
14 stock of such corporation,

15 (B) with respect to a partnership, the single
16 largest share in the profits or capital of such part-
17 nership, and

18 (C) with respect to an estate or trust, the
19 single largest share of the beneficial interests in
20 such estate or trust.

21 For purposes of determining significant ownership in-
22 terest, an interest owned by or for a corporation, part-
23 nership, trust, or estate, or held by a voting trust, shall
24 be considered as owned directly both by itself and pro-

1 portionately by its shareholders, partners, or benefici-
2 aries, as the case may be.

3 (9) The term "motor fuel" means gasoline, diesel
4 fuel, alcohol, and any mixture of any of the foregoing,
5 suitable for use as a fuel in self-propelled vehicles de-
6 signed primarily for use on public streets, roads, and
7 highways.

8 (10) The term "motor fuel service station" means
9 any facility at which motor fuel is sold at retail.

10 (11) The term "sell at retail" means to sell to the
11 general public for ultimate consumption.

12 (12)(A) Except as provided in subparagraph (B),
13 the term "dealer", means a person who occupies as a
14 retailer a motor fuel service station.

15 (B)(i) When used in subsection (b)(2), the term
16 "dealer" means, with respect to a refiner, a person de-
17 scribed in subparagraph (A) who occupies the motor
18 fuel service station under lease or rental agreement
19 with the refiner.

20 (ii) Notwithstanding clause (i), a person described
21 in such subparagraph shall not be considered a dealer if
22 the lease or rental agreement is with a refiner in con-
23 nection with whom such person is a related person re-
24 ferred to in paragraph (2)(B).

1 (13) The term "operate" means, when used in
2 connection with a motor fuel service station, to engage
3 at such station in the business of selling motor fuel at
4 retail through any—

5 (A) employee,

6 (B) commissioned agent,

7 (C) person operating such station pursuant to
8 a contract with a refiner, or

9 (D) person acting on behalf of the refiner or
10 under the refiner's supervision,

11 whose duties include the sale of such motor fuel.

12 (14) The term "person" includes one or more in-
13 dividuals, partnerships, associations, corporations, legal
14 representatives, joint-stock companies, trustees and re-
15 ceivers in bankruptcy and reorganization, common law
16 trusts, and any organized group, whether or not incor-
17 porated.

18 (15) The term "United States" means, when used
19 in a geographic sense, the several States, the District
20 of Columbia, the Commonwealth of Puerto Rico, the
21 Virgin Islands, American Samoa, the Northern Mari-
22 ana Islands, Guam, the Trust Territory of the Pacific
23 Islands, and any other territory or possession of the
24 United States.

1 (e) It shall be the duty of the Federal Trade Commission
2 to commence a civil action for appropriate relief, including a
3 permanent or temporary injunction, whenever any person
4 violates any provision of subsection (a) or (b). Any action
5 under this paragraph may be brought in the district court of
6 the United States for the district in which the defendant is
7 located or resides or is doing business, and such court shall
8 have jurisdiction to restrain such violation and to require
9 compliance.

10 (f)(1) If any person fails to comply with the requirements
11 of this section, any other person directly affected by such
12 failure may maintain a civil action against such person failing
13 to comply with such requirements for damages and appropri-
14 ate equitable relief, including temporary and permanent in-
15 junctive relief. If the plaintiff prevails in any action under this
16 section, the plaintiff shall be entitled to reasonable attorney
17 and expert witness fees to be paid by the defendant, except
18 that in any case in which the court determines that only
19 nominal damages are to be awarded to the plaintiff, the court
20 may, in its discretion, determine not to direct that such fees
21 be paid by the defendant.

22 (2) Such action may be brought, without regard to the
23 amount in controversy, in the district court of the United
24 States in any judicial district in which the principal place of

1 business of such person is located or in which such person is
2 doing business.

3 (g) Subsections (a) and (b) of this section shall take effect
4 one year after the date of the enactment of this Act.

5 REGULATIONS

6 SEC. 3. (a) The Federal Trade Commission shall pre-
7 scribe by regulation the annual date by which the information
8 described in section 2(c)(1) of this Act is required to be pro-
9 vided under such section before the end of the sixty-day
10 period beginning on the date of the enactment of this Act.

11 (b) The Federal Trade Commission shall prescribe any
12 other initial regulations required by the provisions of section
13 2 before the end of the one-hundred-and-eighty-day period
14 beginning on the date of the enactment of this Act.

Senator MATHIAS. Mr. Rasheed.

STATEMENT OF A PANEL, INCLUDING VICTOR RASHEED, EXECUTIVE DIRECTOR, SERVICE STATION DEALERS OF AMERICA, INC., WASHINGTON, DC; JACK W. HOUSTON, EXECUTIVE DIRECTOR, GEORGIA ASSOCIATION OF PETROLEUM RETAILERS, INC., STONE MOUNTAIN, GA; ARTHUR E. PRICE, REVENUE ADMINISTRATOR, MOTOR VEHICLE FUEL TAX DIVISION, ANNAPOLIS, MD; RUDY MOLNAR, MOLNAR'S ARCO, PITTSBURGH, PA; CONRAD JACKSON, HOPKINS SPRINGHILL AVENUE GULF, MOBILE, AL; BRUCE MILEN, PRESIDENT, INTERNATIONAL CARWASH ASSOCIATION/NATIONAL CARWASH COUNCIL, JAX KAR WASH, SOUTHFIELD, MI, AND LLOYD B. ALFORD, FLORIDA STREET CAR WASH, INC., BATON ROUGE, LA

Mr. RASHEED. Thank you, Mr. Chairman, and I would like to thank you for chairing this hearing and also for the opportunity to testify before the distinguished Senator from my home State of Maryland.

Senator MATHIAS. Well, it is a pleasure to have you here.

Mr. RASHEED. Thank you very much.

As this committee meets today to consider the need to limit the control of our major refiners over the domestic gasoline industry, three huge mergers costing nearly \$30 billion, involving several major U.S. refiners, are underway. They signify a new generation of super oil companies in an era of diminishing competition as they acquire new power to control the retail market. One merger, SOCAL/Gulf, will create the largest gasoline marketer in the United States, controlling more than 30,000 retail outlets with over 10 percent of total domestic gasoline sales.

Refiners are also buying up whole chains of unbranded independent retailers to remove yet another source of competition. Last month, Marathon bought out a chain of retail outlets in South Carolina; BP bought out the largest independent marketer in New England, with some 240 outlets.

The shrinking number of competitors and the drift toward monopoly will have its biggest effect on the prices motorists must pay at the pumps in the future. Eventually, the experts predict, there will be only 5 or 6 major refiners instead of 16. These same international oil companies already control the domestic gasoline markets of almost every country in the world today. For example, in neighboring Canada, more than 90 percent of all retail prices are directly controlled by six refiners. Soon, they will be five. In Canada, the largest refiner, Imperial Oil, a subsidiary of Exxon, has retailed gasoline at 25 cents per gallon below the wholesale buying price it charges its own dealers. Others consistently do the same. In the summer of 1982, refiners undercut their dealers by an unbelievable \$1.03 cents per gallon, to force them into a program that would allow the refiners to control their retail prices.

In Canada, as in the United States, oil companies enjoy a profitable method of distribution based on their ability to sell perhaps 70 percent of their gasoline to their captive customer dealers at the highest wholesale price they can impose. The companies then use their company operations to undercut their retailers.

Most surviving dealers in Canada, in order to earn a living, have been forced to become commissioned agents, selling at company set prices. They are no longer independent businessmen.

Canada has been conducting extensive hearings in an attempt to restore competition. A special commission has recommended that dealers should be allowed to purchase cheaper comparable product from any source they can to break the oil companies' captive customer link. Other recommendations include 50 percent divestiture of all retail outlets.

These proposals bear a striking resemblance to the legislation now before you.

In Britain, 90 percent of all high-test gasoline is sold at oil company recommended prices. In Europe, independent dealers and full-service stations have completely disappeared in many areas and have been replaced by totally unattended, company-operated ghost stations. The Governments of Sweden and Japan have appointed commissions to study ways to preserve retail competition. In Australia last July, a railroad strike caused a huge increase in automobile traffic. These same international oil companies outraged motorists by simultaneously increasing the price of gasoline by 25 cents a gallon overnight.

In an effort to restore competition, the Australian Government did pass a divorce law requiring the oil companies to divorce themselves of 50 percent of their company operations. This has not been effective, and there is a strong move now to include the other 50 percent.

Control of the international market is just a step toward achieving control of the American market. This is well on its way. We have seen a decline of 59 percent in the number of refiner-supplied dealers in the past 10 years, with a 36-percent decline in sales, but a 14-percent increase in the number of refiner-operated retail outlets with an 86-percent increase in sales. We have seen nationwide elimination of service from service stations and the immobilization of thousands of automobiles with each cold snap, because many of our former stations with service facilities are either closed or converted into gas only outlets, with convenience stores, selling cookies and milk.

Retail divorce of refiners from the domestic market is a step in preserving retail competition. Six States and the District of Columbia have enacted divorce laws. As far back as 1974, Maryland acted to preserve retail competition and protect the highway safety of its motorists. This decision was upheld unanimously by the U.S. Supreme Court in 1978.

Divorcement in Maryland has benefited the consumer.

Senator MATHIAS. Vic, I am sorry, but your time is up.

Mr. RASHEED. Let me say, Senator, that we urge you to pass this legislation, and we think it will assure a competitive retail gasoline marketplace.

Thank you.

[The following was received for the record:]

TESTIMONY OF

VIC RASHEED

EXECUTIVE DIRECTOR

SERVICE STATION DEALERS OF AMERICA

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE:

AS THIS COMMITTEE MEETS TODAY TO EXAMINE THE NEED TO LIMIT THE CONTROL OF OUR MAJOR REFINERS OVER THE VITAL DOMESTIC GASOLINE INDUSTRY, THREE MERGERS INVOLVING MAJOR U.S. REFINERS ARE UNDERWAY, TO FURTHER DIMINISH COMPETITION AND FOCUS MORE POWER IN THE HANDS OF FEWER AND LARGER OIL COMPANIES.

THESE MERGERS WILL REMOVE THREE COMPETITORS FROM THE WHOLESALE MARKET. ONE MERGER, SOCAL/GULF WILL CREATE THE LARGEST GASOLINE MARKETER IN THE U.S., CONTROLLING MORE THAN 30,000 RETAIL OUTLETS WITH OVER 10% OF TOTAL DOMESTIC GASOLINE SALES.

REFINERS ARE ALSO BUSY BUYING UP WHOLE CHAINS OF UNBRANDED INDEPENDENT RETAILERS TO REMOVE YET ANOTHER SOURCE OF COMPETITION. LAST MONTH, MARATHON BOUGHT OUT A CHAIN OF RETAIL OUTLETS IN SOUTH CAROLINA. BP/SOHIO BOUGHT OUT THE LARGEST INDEPENDENT MARKETER IN NEW ENGLAND WITH SOME 240 RETAIL OUTLETS. GULF OIL AND SUN OIL A FEW YEARS AGO ACQUIRED SEVERAL BIG CHAINS OF OUTLETS IN THE MID-ATLANTIC STATES. THIS SHRINKING NUMBER OF COMPETITORS WILL ULTIMATELY AFFECT THE PRICES MOTORISTS MUST PAY AT THE PUMPS AS THE DRIFT TOWARDS MONOPLY CONTINUES.

THE LARGEST MERGER TO DATE INVOLVES A TAKEOVER OF GULF BY CHEVRON FOR A PRICE OF SOME \$13 BILLION. THIS IS THE FIRST TAKEOVER INVOLVING TWO MEMBERS OF THE SEVEN SISTERS - OUR LARGEST COMPANIES. JUST A FEW WEEKS AGO, THE F.T.C. APPROVED A TAKEOVER OF GETTY BY TEXACO FOR A THEN RECORD \$9 BILLION AND IS NOW SOLICITING COMMENTS. OTHER MAJOR REFINERS REPORTEDLY ARE BUILDING HUGE "WAR-CHESTS" TO PREPARE FOR SIMILAR TAKEOVERS. EVENTUALLY, THE EXPERTS PREDICT, THERE WILL BE ONLY FIVE OR SIX MAJOR REFINERS INSTEAD OF 17. THEIR COMBINED SALES WILL BE CLOSE TO A ONE-HALF TRILLION DOLLARS THIS YEAR.

THESE SAME INTERNATIONAL OIL COMPANIES ALREADY WIELD THE

POWER TO CONTROL THE DOMESTIC GASOLINE MARKETS OF ALMOST EVERY COUNTRY IN THE WORLD TODAY. THEY HAVE TIGHTENED THEIR GRIP ON GASOLINE MARKETS WORLD-WIDE, IN A RELENTLESS MOVEMENT TOWARDS TOTAL CONTROL OF RETAILING. THEY ALREADY CONTROL THE PRICE MOTORISTS PAY FOR GAS IN COUNTRIES FROM CANADA TO AUSTRALIA, FROM JAPAN TO EUROPE. FOR EXAMPLE, IN NEIGHBORING CANADA, MORE THAN 90% OF ALL RETAIL PRICES ARE DIRECTLY CONTROLLED BY SIX REFINERS. SOON THEY WILL BE FIVE.

DIRECT COMPANY-OPERATIONS IN CANADA CONSISTENTLY UNDERSELL THEIR OWN RETAILERS, AS THEY DO HERE. IN CANADA, THE LARGEST REFINER, IMPERIAL OIL - A DIRECT SUBSIDIARY OF EXXON - HAS RETAILED GASOLINE AT 25 CENTS PER IMPERIAL GALLON BELOW THE WHOLESALE BUYING PRICE IT CHARGES ITS OWN DEALERS. THIS IS NOT UNUSUAL. OTHERS CONSISTENTLY DO THE SAME. IN THE SUMMER OF 1982, REFINERS UNDERCUT DEALERS BY AN UNBELIEVABLE \$1.03 PER IMPERIAL GALLON, TO FORCE THEM INTO A SUBSIDY OR CONSIGNMENT PROGRAM THAT WOULD ALLOW THE REFINERS TO CONTROL THEIR RETAIL PRICES.

IN CANADA, AS IN THE U.S., THE OIL COMPANIES ENJOY A PROFITABLE METHOD OF DISTRIBUTION BASED ON THEIR ABILITY TO SELL PERHAPS 70% OF THEIR GASOLINE TO THEIR CAPTIVE-CUSTOMER-DEALERS OR AGENTS, AT THE HIGHEST WHOLESALE PRICE THEY CAN IMPOSE. THE DEALER'S PRICE, OF COURSE, DETERMINES THE PRICE HIS CUSTOMERS, THE MOTORISTS, MUST PAY. THE COMPANIES THEN USE THEIR DIRECT COMPANY-OPERATIONS AS CUT-RATE OUTLETS IN COMPETITION WITH THEIR FRANCHISEES.

SURVIVING DEALERS IN CANADA EXIST STRICTLY AT THE PLEASURE OF THEIR REFINERS. IN ORDER TO EARN A LIVING, MOST HAVE BEEN FORCED TO BECOME COMMISSIONED AGENTS SELLING AT COMPANY-SET PRICES. THEY ARE NO LONGER INDEPENDENT BUSINESSMEN. FOR EXAMPLE, IN WINDSOR, ONTARIO, ACROSS FROM DETROIT, LESS THAN A DOZEN INDEPENDENT DEALERS REMAIN OUT OF 112 LOCATIONS. A RECENT SURVEY SHOWED THAT OIL COMPANIES NOW CONTROL PRICES IN 93% OF THE LOCATIONS IN WINDSOR.

THE RESTRICTIVE TRADE PRACTICES COMMISSION OF CANADA HAS BEEN CONDUCTING EXTENSIVE HEARINGS INTO THE STATE OF COMPETITION IN ITS PETROLEUM INDUSTRY. ONE RECOMMENDATION, MADE TO THE CANADIAN GOVERNMENT EARLIER THIS MONTH, WAS THAT DEALERS SHOULD BE ALLOWED

TO PURCHASE CHEAPER, COMPARABLE PRODUCT FROM ANY SOURCE HE CAN, BREAKING THE OIL COMPANIES' CAPTIVE-CUSTOMER LINK. OTHER RECOMMENDATIONS TO INCREASE COMPETITION HAVE INCLUDED 50% DIVESTITURE OF RETAIL OUTLETS. THESE PROPOSALS BEAR A STRIKING RESEMBLANCE TO THE LEGISLATION NOW BEFORE YOU.

MY REFERENCE TO THE LACK OF COMPETITION IN THE CANADIAN MARKET IS TO POINT OUT TO YOU THAT IT WAS CREATED BY THOSE SAME INTERNATIONAL OIL COMPANIES THAT WE CONSIDER TO BE AMERICAN OIL COMPANIES. ALSO TO POINT OUT THAT THIS IS NOW AN INTERNATIONAL METHOD OF OPERATION.

IT IS THE SAME SITUATION IN BRITAIN WHERE 90% OF ALL HIGH TEST GAS IS SOLD AT OIL COMPANY RECOMMENDED PRICES. IT IS THE SAME IN EUROPE WHERE INDEPENDENT DEALERS AND FULL-SERVICE STATIONS HAVE DISAPPEARED IN MANY AREAS AND ARE BEING REPLACED BY TOTALLY UNATTENDED, COMPANY-OPERATED GHOST STATIONS.

THE GOVERNMENTS OF SWEDEN AND JAPAN HAVE APPOINTED COMMISSIONS TO STUDY THE INTERNATIONAL MARKET TO TRY AND PRESEERVE RETAIL COMPETITION IN THEIR COUNTRIES. IT IS THE SAME IN AUSTRALIA.

LAST JULY, A RAILROAD STRIKE CAUSED A HUGE INCREASE IN AUTOMOBILE TRAFFIC. THESE SAME OIL COMPANIES OUTRAGED MOTORISTS BY SIMULTANEOUSLY INCREASING THE PRICE OF GASOLINE BY 25 CENTS PER GALLON OVERNIGHT.

THEY WERE ABLE TO DO THIS BECAUSE OF THEIR CONTROL OVER THE RETAIL LOCATIONS. IN AN EFFORT TO RESTORE COMPETITION THE FEDERAL GOVERNMENT DID PASS A DIVORCEMENT LAW REQUIRING THE OIL COMANIES TO DIVORCE THEMSELVES OF 50% OF THEIR COMPANY-OPERATIONS. THIS HAS NOT BEEN EFFECTIVE AND THERE IS A STRONG MOVE TO INCLUDE THE OTHER 50%.

CONTROL OF THE INTERNATIONAL MARKET IS ONLY THE FIRST STEP TOWARDS ACHIEVING TOTAL CONTROL OF THE BIG ONE - THE AMERICAN DOMESTIC PETROLEUM MARKET. THIS IS WELL ON ITS WAY. WE HAVE SEEN A DECLINE OF 59% IN THE NUMBER OF REFINER SUPPLIED DEALERS IN THE PAST 10 YEARS WITH A 36% DECLINE IN SALES. A 14% INCREASE IN THE NUMBER OF REFINER-OPERATED RETAIL OUTLETS WITH AN 86% INCREASE IN SALES. OUR NEXT WITNESS, MR. HOUSTON, WILL TELL YOU HOW THIS WAS DONE.

WE HAVE SEEN A NATIONWIDE ELIMINATION OF SERVICE FROM SERVICE STATIONS AND THE IMMOBILIZATION OF THOUSANDS OF AUTOMOBILES WITH EACH COLD SNAP BECAUSE MANY OF OUR FORMER STATIONS WITH SERVICE FACILITIES ARE EITHER CLOSED OR CONVERTED INTO GAS-ONLY OUTLETS WITH CONVENIENCE STORES, SELLING COOKIES AND MILK.

RETAIL DIVORCEMENT OF REFINERS FROM THE DOMESTIC MARKET IS A STEP IN PRESERVING RETAIL COMPETITION. SIX STATES AND THE DISTRICT OF COLUMBIA HAVE ENACTED DIVORCEMENT LAWS. GEORGIA HAS JUST PASSED A SIMILAR BILL. THE OLDEST EXAMPLE OF AN EFFECTIVE RETAIL DIVORCEMENT LAW, IS IN THE STATE OF MARYLAND. AS FAR BACK AS 1974, MARYLAND ACTED TO PROTECT THE HIGHWAY SAFETY OF ITS MOTORISTS BECAUSE IT NOTED AN OIL COMPANY TREND TO ELIMINATE SERVICE FACILITIES, ALSO TO PRESERVE RETAIL COMPETITION. THIS DECISION WAS UPHELD UNANIMOUSLY BY THE U.S. SUPREME COURT IN 1978. HOWEVER IN AN ATTEMPT TO DISCREDIT THE LAW, ONE OIL COMPANY HAS SPENT A MILLION DOLLARS, COMMISSIONING "STUDIES" PURPORTING TO SHOW THAT GASOLINE PRICES ROSE IN MARYLAND AS A RESULT OF DIVORCEMENT, THE TRUTH IS THAT MARYLAND PRICES ARE CONSIDERED TO BE AMONG THE MOST COMPETITIVE ON THE EAST COAST.

A QUICK DRIVE THROUGH NEARBY MARYLAND WILL CONFIRM THIS.

DIVORCEMENT IN MARYLAND HAS BENEFITTED THE CONSUMER. IT HAS RESULTED IN INTENSE RETAIL COMPETITION, MODERN WELL-EQUIPPED SERVICE FACILITIES OPERATED BY SECURE DEALERS WILLING TO MAKE LARGE CAPITAL INVESTMENTS IN THEIR LOCATIONS. IT HAS ALSO BENEFITED THE REFINERS. WHEN DIVORCEMENT WAS IMPLEMENTED IN MARYLAND IN 1979, EXXON TURNED OVER 43 COMPANY-OPERATED OUTLETS OVER TO DEALERS. THEIR INCREASED SALES PERFORMANCE INSPIRED THE COMPANY (ALTHOUGH IT MAY NEVER ADMIT IT) TO CONVERT SEVERAL HUNDRED COMPANY OPERATIONS BACK TO DEALER-OPERATION IN THE NEXT TWO YEARS.

SIMILARLY, THE PRESIDENT OF AMOCO TESTIFIED BEFORE A CONGRESSIONAL HEARING A FEW YEAR AGO THAT HIS COMPANY COULD NOT OPERATE RETAIL OUTLETS AS EFFECTIVELY AS INDEPENDENT DEALERS DO. YET TO EXTEND THEIR CONTROL OVER THE RETAIL MARKET, OIL COMPANIES PERSIST IN TRYING TO DRIVE THEIR FRANCHISEES OUT OF BUSINESS. THEY CAN DO THIS NOT BECAUSE THEY ARE MORE EFFICIENT AT MARKETING,

BUT BECAUSE THEY ARE THE DEALERS' LANDLORDS AND FRANCHISORS, AND BECAUSE THEY ARE MONOPOLY SUPPLIERS TO THE BRANDED STATIONS.

WE BELIEVE THAT THE DIVORCEMENT AND OPEN SUPPLY PROVISIONS OF S.40 WILL RESTORE HEALTHY COMPETITION AT THE RETAIL LEVEL OF THE GASOLINE INDUSTRY. THESE PROVISIONS WILL OPEN UP 100,000 GAS STATIONS FOR PRICE COMPETITION AT THE WHOLESALE LEVEL, AND THAT CAN ONLY MEAN LOWER PRICES FOR RETAIL CUSTOMERS.

WE URGE YOU TO PASS THIS LEGISLATION AND HELP ASSURE A COMPETITIVE RETAIL GASOLINE MARKETPLACE. THE TIME TO ACT IS NOW, BEFORE THE REFINERS FURTHER CONSOLIDATE THEIR GRIP ON THIS VITAL INDUSTRY.

Senator MATHIAS. Mr. Houston.

STATEMENT OF JACK W. HOUSTON

Mr. HOUSTON. Mr. Chairman, thank you very much for allowing us to appear today.

I am here to tell you that the refiners are continuing to lessen competition and to destroy competitors in the marketplace. In summary, it boils down to simply this. When refiners fix the wholesale price, when refiners control the supply, when refiners fix the occupancy cost of retail locations and then fail to cover these same costs that are imposed on the retail dealers, then they are massively destroying their competitors in the market system.

While on the one hand, they are pushing up costs—costs which they control on retail dealers—on the other hand, they are lowering the price to the consumer in their own retail pump locations. They are acting not as a competitor, but as a predator in the marketplace, and a competitor could not invoke such cost upon his own competitors.

That is an important point to consider, in my opinion.

We have, on page 4 of the written testimony, a survey that was taken January 3, 1984 in Atlanta, GA with the Texaco stations. In that instance, a quick look at that survey will show that there is as much as an 18-cents-below-cost selling taking place in the Metropolitan Atlanta market today, or was on January 3, and it is continuing today. And the more significant point, perhaps, to be taken from this survey is that consumers who are buying from retail dealers are paying an excessively higher price for product than they should have to pay. Refiners have consistently said they are not selling below cost in their own company stations. Therefore, they must be overcharging the retail dealers. They are overcharging not only in the wholesale price; they are overcharging in occupancy costs. They are overcharging in credit card surcharge costs and other costs which they can control on the competitor. And it is a deliberate effort to destroy the competitor in the marketplace and to destroy competition.

We believe that prices to consumers will be lowered if, in fact, divorcement laws are placed on the books. And it was, I believe, for that simple statement that the Georgia lawmakers on the 21st of February enacted a divorcement law in the State of Georgia. It is subject, of course, to the Governor's signature in the next few days. We hope that he is going to sign it and believe that he will

But that is a step in the right direction, of a State taking action. I submit to you, Mr. Chairman, that the actions of Georgia and the actions of the other States previously adopting such legislation, and some 20 States now looking at this issue, that this is a national problem, that this is a problem that cannot be ignored by the Congress, that S. 40 ought to be passed, should be passed, as quickly as possible, in order to give some uniformity to the application, but more importantly, instead of waiting for some dealers in some States to be choked out of the business and too late to recover or to save them, it is time for Congress to act in order to put the house in order with regard to competition in the retail marketplace in the gasoline industry.

I urge your immediate passage of S. 40.

Senator MATHIAS. Thank you very much.

[The following was received for the record:]

S.40

THE SMALL BUSINESS MOTOR FUEL MARKETER PRESERVATION ACT

UNITED STATES SENATE, JUDICIARY COMMITTEE

STATEMENT BY

JACK W. HOUSTON

ON BEHALF OF

THE GEORGIA ASSOCIATION OF PETROLEUM RETAILERS, INC.

AND THE

SERVICE STATION DEALERS OF AMERICA, INC.

March 14, 1984

My name is Jack W. Houston and I am appearing here on behalf of the Georgia Association of Petroleum Retailers and the Service Station Dealers of America in support of S.40, a bill seeking "simple fairness" and "justice" in the marketing of petroleum products.

I have represented retail dealers for almost 28 years. I co-authored the book "THE CASE FOR LEGISLATIVE RELIEF FROM THE IMPENDING DESTRUCTION OF SMALL BUSINESS AND COMPETITION IN THE GASOLINE INDUSTRY" (1980) and three separate editions of "Questions & Answers" dealing with this type legislation (1981, 1982, 1984).

I have been found by a United States District Court to be an expert witness in my field after giving testimony that was "... credible and believable and acceptable as an expert opinion".

Surely the time has arrived to move from investigations, hearings, and developing an ever larger congressional record about the unfair anticompetitive behavior of certain refiners of motor fuels. The vast record amassed is complete except for adding the immediate past evidence to the heap.

Passage of S.40 must come soon or it will be too late - the final curtain will have fallen too low to raise again and reestablish real competition in gasoline marketing.

WHY SO PESSIMISTIC A VIEW?

Refiners are earning less and less on sales at retail in company-operated outlets than the refiners earn on sales at wholesale to their retail dealers.

If allowed to continue their anticompetitive marketing practices the refiners will continue to lessen and destroy competition.

In summary, refiners control and fix the wholesale price their competitors must pay; control available sources of product supply; fix occupancy cost of stations operated by their competitors; impose other demands that increase costs of doing business by competitors; and refiners then fail to recover those same costs when pricing gasoline on retail pumps at their own company-operated outlets.

Pushing upward costs of doing business on the one hand at the competitors' outlets while lowering retail prices on the other hand at company-stores is an act of predators, not something true competitors can do.

IS THERE CONTINUING HARD EVIDENCE THAT REFINERS ARE ENGAGED IN SUCH ACTS OF UNFAIRNESS?

In Atlanta, Georgia I ordered a private survey on January 3, 1984 to obtain the facts. Here is what I found:

HARD EVIDENCE SUPPORTS PASSAGE OF S.40

Data collected from 40 Texaco retail locations identified as self-serve facilities on a Texaco map of Atlanta and Vicinity revealed that 33 of the locations are being operated as company stores by Texaco.

The data showed:

	regular leaded	regular unleaded	premium unleaded
Texaco's Average Retail Price per Gallon	103.23¢	113.27¢	126.05¢
Texaco's Lowest Retail Price per Gallon	99.9¢	110.9¢	121.9¢
Texaco's Highest Retail Price per Gallon	107.9¢	119.9¢	128.9¢
THIS IS THE COST fixed by Texaco: (to dealer operated stations)			
Texaco's Wholesale Price charged dealers	101.55¢	105.55¢	111.55¢
Texaco's Occupancy charge for comparable stations offered to dealers, based on 100,000 gal. Mo. sales	5.00	5.00	5.00
Texaco's Credit Card Surcharge on dealers, based on 50% of sales on credit X 3%	2.00	2.00	2.00
Texaco's Hourly Contract rate paid to personnel to operate company-operated stations, based on \$7 hr., sales of 100,000 gal. mo.	<u>5.30</u>	<u>5.30</u>	<u>5.30</u>
LAID-IN COST* For Texaco, based on what Texaco charges Texaco retail dealers	113.85	117.85	123.85
Plus 4% Tax on Retail Price	<u>4.25</u>	<u>4.41</u>	<u>4.65</u>
TOTAL LAID-IN Cost plus 4% Tax	<u><u>118.10¢</u></u>	<u><u>122.26¢</u></u>	<u><u>128.50¢</u></u>

* Does not include insurance, utilities, and other cost to Texaco to operate retail outlets.

TEXACO IS EARNING LESS ON SALES AT RETAIL THAN IT EARNS ON SALES AT WHOLESALE TO ITS RETAIL DEALERS.

TEXACO'S UNFAIR ANTICOMPETITIVE MARKETING PRACTICES ARE "PREDATORY" AND IF ALLOWED TO CONTINUE WILL LESSEN AND DESTROY COMPETITION.

FOOTNOTES TO "HARD EVIDENCE"

Footnote No. 1 - The data used to support the above information was collected January 3, 1984 by a private contractor hired by GAPR to conduct on-site research at all self-serve Texaco locations shown on the special traffic map of Atlanta and vicinity available at most Texaco stations.

Footnote No. 2 - The best scenario if all dealers qualify for incentive rebates that would reduce wholesale prices place the average reduction at no more than 3¢ a gallon. Consideration of the 3¢ lower wholesale price does not alter significantly the above facts and findings. Some retail dealers do not enjoy the 3¢ reduction.

Divorcement and Open Supply will increase the value and the range of consumer choice. History has proven that the more competitors in a market system greater the competition and lower the price to consumers.

Competition based on skills, abilities and quality services as well as price produces the greater value to consumers. A hand-full of refiners controlling retail prices will not produce the same values for consumers.

Times have become more desperate. For the very first time the Georgia Oilmen's Association, jobbers in the State of Georgia, and the Georgia Association of Petroleum Retailers climbed upon the same tree stump and shouted the same song to Georgia lawmakers. Our mutual cries for "simple fairness" were heard.

Senate Bill 367 as passed the Georgia General Assembly
February 21st, 1984 requires that:

After July 1, 1984, gasoline refiners cannot open any more retail gasoline service station outlets and operate them as company stores.

All retail outlets opened and operated by a refiner after February 20 and before July 2, 1984, will have one year for the refiner to lease the stations to dealers.

A refiner will have a temporary right to operate a retail outlet to avoid closing the outlet for a period not to exceed 365 days.

All refiners with company-operated retail outlets operating as of February 20, 1984, will have the right to continue to operate as company-stores.

The Governor will decide next week the fate of that legislation. But with a vote of 112 to 51 in the House of Representatives and 45 to 7 in the Senate and after seven years of hearing our pleas for relief we expect the Governor to sign that legislation into law.

Grandfathering existing refiner-operated retail outlets into the law gives the refiners an opportunity to clean up their act in Georgia to avoid further legislative remedies.

The refiners should lower wholesale prices to their dealers and to their jobbers, who service other retail dealers, to permit the retailers to compete with company-operated outlets; unless, the refiners are incurring a loss by selling at retail below costs they charge dealers at wholesale. The refiners have claimed they are not selling below cost. Lowering the price to the dealers is a matter of simple fairness to enhance competition in the retailing of gasoline ... and it is a matter of fairness that they stop overcharging consumers who support their dealer network.

One of the more active jobbers who worked closely with us wrote the Governor a letter about signing into law the pending bill (S.367). Three paragraphs have particular significance to our plea today. I quote them verbatim with his permission as follows:

"Divorcement type legislation was first talked about in Georgia in 1978. At that point most jobbers, including me, could not imagine conditions as they are today. So we and the refiners opposed it, and it did not pass. Only this year have the dealers and jobbers united to try to pass this type legislation in the form of S.B.367. Both the Georgia Association of Petroleum Retailers (dealers) and the Georgia Oilmen's Association (jobbers)

have endorsed and worked hard to bring it to your desk. It has also been introduced in 22 other state legislatures. It has already passed into law by 5 states. The first of which was Maryland. S.B. 367 tracks almost exactly the Maryland Law which has been ruled Constitutional by the U.S. Supreme Court.

We think this may be our last chance to have this law passed.
Many of our fellow jobbers have been threatened and intimidated
by the refiner who sells them, to a point where they are afraid
to stand up. This can only get worse as their financial condition
worsens. Also, most of the major refiners have announced plans to build many more direct units in Georgia. With Texaco trying to buy Getty Oil for eight billion dollars and Arco trying to buy Gulf for thirteen billion, you can see the size of our opposition.

The talk that bothers me the most is the talk which says the consumer will be better off with a few Multi-National Refiners left to set the retail price of gasoline, than he is now with many local dealers and jobbers competing for his business. There is ample evidence throughout the world to show what happens when all industry ends up in a few hands."

(underscoring added)

Excerpted from Letter to Governor Harris
 dated 3-5-84 from Edgar Blalock, Jr.
 Blalock Oil Company
 Jonesboro, Ga.

Mr. Chairman, there are other considerations than preservation of competition and small business in gasoline marketing that should be examined. These additional considerations are also very important to consumers:

- 1) Loss of job opportunities for Americans that need it most;
- 2) Loss of essential fast and economical services needed by each community throughout this Nation;

3) Loss of economic values to local communities;

4) Loss of ability, comfort and convenience of American motorists to travel with confidence that essential minor mechanical services as well as gasoline will be readily accessible as needed without extreme delay and at reasonable prices.

Perhaps Georgia and the other States (Maryland, Connecticut, Delaware, Virginia, and Washington, D.C.) have turned the tide of the onrushing slaughter of competition and small business in gasoline marketing that's caused by the refiners' unfair anticompetitive marketing practices. But don't you agree, with some twenty states looking at similar legislation, that the Congress of the United States needs to get on with its responsibility to provide corrective legislative relief on such a national problem?

The time has arrived to act. I urge you to send S.40 to a successful vote on the Senate Floor.

Mr. Chairman, thank you for allowing me this time. I would ask that the attached "27 Questions and Answers" I have prepared be entered in the official record as a part of my testimony.

If there are any questions it will be my pleasure to respond.

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27

QUESTIONS

AND

ANSWERS

S.40 and H.R.1755

(97th Congress: S.326 and H.R.1362)

SMALL BUSINESS MOTOR FUEL MARKETER PRESERVATION ACT

98th Congress, 2nd Session

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INTRODUCTION

"Congress is at a critical juncture regarding the structure of competition in the petroleum industry. We are either going to have a highly competitive gasoline industry or else one dominated by a few large integrated petroleum companies. If Congress desires to preserve for future generations a highly competitive gasoline industry, then it must act quickly for the structure of competition in this industry is on the brink of ruin."*

"The Final Curtain Is Falling on Dealers, And Competition In The Marketing of Motor Fuel."†

"Traditionally, Shell has relied on Independent Dealers and jobbers as they provide the most efficient and competitive means of distribution, most of our automotive gasoline."‡

OPEN SUPPLY "... provisions of the bill prohibiting producers or refiners from restraining, interfering with, or in any way preventing, the dealer-operator from purchasing alternative sources of supply, and reselling the same to the public (with adequate disclaims of brand name),... could be highly procompetitive."§

*Copyright 1980 -- "The Case For Legislative Relief From The Impending Destruction Of Small Business And Competition In The Gasoline Industry", Page 63.

†Copyright 1981 -- "20 Questions & Answers, H.R.1362 & S.326."

‡Shell Oil Company Comments, ERA, August 19, 1980 (underscoring added for emphasis.)

§Federal Trade Commission, Bureau of Competition, Assistant Director, Ronald B. Rowe, before subcommittees of House Small Business Committee on H.R. 6722, May 20, 1980. (Underscoring added.)

27 QUESTIONS & ANSWERS ON THE
SMALL BUSINESS MOTOR FUEL MARKETER
PRESERVATION ACT
S.40 & H.R. 1755

1. Q. WHAT ARE THE KEY PROVISIONS OF S.40 AND
H.R.1755?

A. Divorcement

The sixteen largest integrated refiners will be prohibited from directly or indirectly operating any retail gasoline outlets. They will be permitted to continue ownership of retail properties and leasing of same to dealers.

Open Supply

It would be unlawful for anyone to interfere with the right of a dealer to purchase, store or sell motor fuel products obtained from anyone else provided it is not available from the regular supplier upon terms and conditions reasonably comparable to those available to the dealer from any other such persons.

2. Q. WHY IS SUCH LEGISLATION NECESSARY?

A. To Preserve Competition! The destruction of small business and competition is in an advancing stage. Unless stopped now, the result will be irreparable damage to the structure of competition in the gasoline industry.

Some refiners are: taking advantage of their power as suppliers, practicing price discrimination by charging their dealers artificially higher prices than they charge other retailers who compete with the dealers, and transferring product to such company stores at prices which are less than the prices these suppliers charge their dealers, selling gasoline at retail in the company stores at a price that does not cover the wholesale price charged their dealers

and the cost of operating the company store retail outlets, etc.

3. Q. WILL DIVORCEMENT OF THE SIXTEEN REFINERS FROM RETAILING REDUCE TRUE COMPETITION TO THE DETRIMENT OF CONSUMERS?

- A. No! Since refiner direct (employee-operated) stations do not depend on their individual profitability to remain in business (instead they are supported by upstream profits in crude oil production and refining), their selling prices can be manipulated. Thus, a refiner (or group of refiners operating individually but nevertheless on a common path) could choose to price at retail below or only slightly above the buying (wholesale) price of independent retail dealers (as some refiners have done) and ultimately force these small independent retailers out of business (as thousands have been since the shortage in 1973). Once the independent dealers are removed from the marketplace, the refiner(s) could then charge retail prices much higher than would have been the case under fair competitive practices and recover all lost profits while controlling the entry of new firms into the marketplace by denying them supplies of gasoline.

In fact, this is exactly what has happened in today's marketplace. If allowed to continue, this practice will detrimentally affect consumers by forcing true competition out of the marketplace.

Not only do these unfair practices narrow consumer choice and the benefits of competition, they also are destroying the network of dealer stations that offer minor mechanical services at the lowest cost and with the greatest convenience. If refiners are allowed to continue to engage in unfair marketing practices, consumers will find that fewer stations mean fewer

competitors, higher gasoline prices and a lack of mechanical services and other conventional services associated with full service dealer operated stations.

4. Q. WILL DIVORCEMENT AND OPEN SUPPLY PROVISIONS REMOVE THE INCENTIVE FOR JOBBERS TO CONTINUE WHOLESALE OPERATIONS?

A. No! The wholesale function of distributing motor fuel is essentially a service business, i.e., it provides storage, transportation and availability functions in addition to quantity purchasing, credit and equipment which it may furnish for the customers. Thus to the extent that a jobber provides these services better or cheaper than the customer can itself provide them, the customer will buy from the jobber.

5. Q. DO EXISTING LAWS (SHERMAN, CLAYTON, ROBINSON-PATMAN, FTC AND THE PETROLEUM MARKETING PRACTICES ACTS) ALREADY AFFORD DEALERS EFFECTIVE PROTECTION AGAINST THE ANTI-COMPETITIVE MARKETING PRACTICES WHICH THE DIVORCEMENT AND OPEN SUPPLY PROVISIONS WILL CORRECT?

A. No! These existing laws are not effective for a variety of reasons. For example, the intra-company transfer of motor fuel by a refiner (or jobber) to direct employee-operated retail stations is not a sale and therefore is not covered by existing laws. Also, the Petroleum Marketing Practices Act only provides protection regarding notification, termination, cancellation, or refusal to renew or enter a new contract. Furthermore, the great number of direct operated stations make it easy for refiners (and jobbers) to escape the provisions of the Robinson-Patman Act and defend their predatory pricing practices by pointing to the other's

marketing methods as a good faith meeting of competition.

6. Q. WHAT EFFECT WILL DIVORCEMENT AND OPEN SUPPLY PROVISIONS HAVE ON RETAIL PRICES?

- A. Favorable! Because substantially more stations will be in the business of offering sales of gasoline and other services to consumers, there will be increased competition and therefore lower prices than would result under market conditions where only a few firms were available to meet the demands of consumers. There will be no increase in the average retail price charged consumers as a result of this legislation. In fact, with the introduction of fair pricing and the end of refiner and jobber's present restricted practices toward dealers, the consuming public will benefit by receiving lower prices overall.

Not only will the consumer benefit from a price standpoint, the more dealers in a market area result in increased competition to attract and hold consumer patronage by offering the greatest overall value at the lowest price -- or in other words, better service at real service stations.

7. Q. OPEN SUPPLY —

- a. Will it "force Shell (and others) out of the branded gasoline business?
- b. Will it "irreparably harm" branded retailers?
- c. Will it "substantially alter gasoline marketing?
- d. Will it "have a significant impact on Shell" (and others)?

These four questions were raised in Shell's letter to its dealers dated December 4, 1981. The following answers are responses to Shell but are also applicable to all refiners.

- A. a. Open Supply will not force Shell or any other major oil company out of the branded gasoline business.

Open supply merely establishes a basic and clear right for a (Shell) branded retailer to purchase another company's lower priced gasoline, to store in existing underground tanks, to use existing dispensing pumps, etc. (for which most dealers pay an economic rent -- a fair return on investment is earned by such oil companies that charge economic rents) provided that Shell is notified and is given the opportunity to meet the lower price by offering Shell gasoline to the Shell dealer at a reasonable comparable wholesale price.

Shell will continue to have the right to insist upon Shell retailers selling only Shell gasoline by staying competitive in wholesale prices.

Shell would make the choice whether it would or would not remove its gasoline from any retailer by its decision to meet or not to meet competition.

- b. Open Supply will not irreparably harm branded retailers.

Open Supply will help branded retailers meet price competition from another branded retailer or an unbranded retailer that is causing a reduction in the number of gallons sold and the volume of other products and services sold by branded retailers.

Shell contends dealers can now buy non-Shell gasoline. Open Supply would remove Shell's rule "to de-identify your station" and would allow dealers to de-identify one or more pumps without loss of the right to continue selling through remaining pumps under the Shell trademark.

c. Open Supply will not alter gasoline marketing.

Shell's charge is a hollow threat to remove brand identity. Nationally recognized trademarks and profits therefrom are a way of life that Shell and other major integrated oil companies could ill-afford to scrape. Offering equitable wholesale prices to retailers for branded gasoline to comparably meet lower prices for similar (unbranded) gasoline will enhance sales (and profits) of branded products and maximize consumer patronage of Shell products.

d. Open supply will not significantly impact on Shell.

Open Supply will not impair the value of the trademark. Making another product or if Shell wishes Shell products available at lower prices certainly will improve consumer appreciation and recognized value of the Shell Trademark. The Open Supply provision requires proper notice to consumers on dispensing pumps when other than a Shell product would be sold. Shell's trademark would thus be protected and consumers would be protected from deception. Consumers would have no trouble identifying the source of a product quality problem.

Dealers are responsible small business persons capable of complying with Octane Posting requirements, controlling the delivery to avoid leaded fuel being mixed with unleaded fuel. Consumers likewise are capable of understanding availability of another product on the same property with a Shell product where there is the required notification posted on a dispensing pump.

Shell dealers will be given the right under Open Supply to seek out one or more lower

priced good quality (sometimes same brand) product with which to meet competition when Shell itself is unwilling to be competitive with its wholesale prices to dealers.

8. Q. WHAT IN ADDITION TO HIGHER PRICES DO CONSUMERS STAND TO LOSE IF DIVORCEMENT AND OPEN SUPPLY PROVISIONS ARE NOT ENACTED INTO LAW?

A. Convenient Access to Service! Consumers will lose the convenience of trading with a local dealer who is in business to meet his total automotive needs -- from gasoline to tune-ups to minor and major repairs. Full service dealers will not be available to provide the fast, convenient, and lower cost minor mechanical services, which the consumer knows to be the most effective involving the least loss of time and the lowest overall cost.

9. Q. WHAT EFFECT WILL ENACTMENT OF DIVORCEMENT AND OPEN SUPPLY HAVE ON MOTOR FUEL (PARTICULARLY GASOLINE) SUPPLY AVAILABILITY?

A. None! Refiners have historically earned good profits upstream from retailing in crude oil, production, and refining. In fact retailing is considered a drain on a refiner's upstream profits, in a competitive marketplace; and, their stockholders should not tolerate a major sector of the firm which does not earn an adequate return on its investment. If this were clearly known to the average stockholders, they would insist that a firm remove itself from retailing and devote its best efforts to those parts of the firm's business that will earn a higher return. Thus an emphasis on production and refining to maximize a refiner's return will result in adequate supplies being available to the public and probably at a lower cost otherwise.

10. Q. WILL ENACTMENT OF DIVORCEMENT AND OPEN SUPPLY LIMIT ENTRANTS TO THE RETAIL MARKET OR PROTECT INEFFICIENT DEALERS?

A. No! To the contrary, easier entrance will be encouraged and improved competitive conditions will be experienced for the consumers' benefit. There is nothing in the legislation that provides any assurance any dealer will remain in business ... only that all dealers will have a basic and reasonable fair opportunity to compete. The more efficient dealers will survive and the inefficient will not survive.

11. Q. WHAT EFFECT WILL ENACTMENT OF DIVORCEMENT AND OPEN SUPPLY HAVE ON (1) EMERGENCY ROAD SERVICES; (2) MINOR MECHANICAL REPAIR SERVICES AT GASOLINE STATIONS; (3) ON SENIOR CITIZENS, WHO ARE ON FIXED INCOMES; AND (4) DISABLED PERSONS, WHO MUST HAVE FULL SERVICE AVAILABILITY, AS WELL AS THE GENERAL POPULATION OF MOTORISTS, WHO EXPERIENCE A NEED FOR AND MUST HAVE THE AVAILABILITY OF THESE SERVICES?

A. A Positive Effect! Unless fairness is restored so as to permit and enable full service (and self-serve) dealer operated stations to compete in motor fuel (gasoline) sales, services with gasoline will disappear and the comfort, convenience and ability of consumers to travel by automobile will be seriously handicapped by extreme delays and higher costs. The public safety and welfare will be adversely affected. Senior citizens and the disabled will not be able to obtain needed services at low prices at conveniently located stations throughout America.

12. Q. DID THE UNITED STATES SUPREME COURT REJECT THE MARYLAND STATE DIVORCEMENT LAW AS ANTI-COMPETITIVE?

A. No! The Court said the same thing about the Maryland State Divorcement Law as it had said

about the Robinson-Patman Act ... that the Court was not ruling on the wisdom of the law or whether it was anti-competitive in its opinion, but only that it was constitutional to enact such law to provide relief from practices the Maryland State Lawmakers considered to be wrong.

13. Q. WHAT STATES HAVE ALREADY ENACTED LAW TO STOP THE UNFAIRNESS OF REFINER AND JOBBER EMPLOYEE-OPERATED STATIONS?

- A. Washington, DC -- Effective January 1, 1981 Refiner operation of retail stations are prohibited;
Maryland and Connecticut -- Divorced Refiners from employee-operated retail stations;
Delaware -- Prohibits refiners from employee-operated retail stations (exception -- on turnpikes);
Virginia -- Declared moratorium on refiner employee-operated stations;
Georgia -- Divorces Refiners from company-operating retail stations opened after February 20, 1984; Prohibits refiners from opening any more retail stations after July 1, 1984; Permits refiners with company-operated retail outlets open and operating as of February 20, 1984 to continue in operation. (Passed Georgia Legislature 2/21/84 112 to 51 House of Representatives; 45 to 7 Senate. Awaiting Governor's consideration.)

Prohibits jobbers from selling at retail in their employee-operated retail stations any gasoline the jobber purchased as a jobber at jobber discounts (Constitutionality test final - See 5th Circuit/Certiorari denied - found constitutional. State Superior Court Order is pending -- on appeal.).

14. Q. ARE REFINERS TRUE COMPETITORS AT RETAIL?

- A. No! Because they control wholesale supplies to dealers, control wholesale prices charged dealers, and control dealers who are required by contract to purchase that product. Some refiners have used their upstream advantage to compete with dealers at retail by selling at retail at a price that does not cover the wholesale price charged dealers and the cost of employee-operating the retail stations. These refiners are not competitors in the true sense. They are predators (either intentional or not) engaged in unfair marketing practices and they are destroying competition and small business in the gasoline industry.

15. Q. WHAT EFFECT WILL DIVORCEMENT AND OPEN SUPPLY HAVE ON EMPLOYMENT OPPORTUNITIES AND THE ECONOMY?

- A. A Positive Effect! Job opportunities will be preserved and will increase for skilled, semi-skilled and unskilled workers, for young people needing part-time or full time employment, and for small business entrepreneurship opportunities. The local and national economy will be benefitted advantageously.

16. Q. IS DIVORCEMENT NECESSARY IN ADDITION TO THE OPEN SUPPLY PROVISIONS?

- A. Yes! Divorcement is necessary to protect the marketing segment of the oil industry from the excessive control by a few refiners who would control marketing as they now control all other segments ... they control: 93% of the Nation's proven domestic crude oil; 80% of refining capacity; 90% of crude oil pipelines; and more than 75% of the finished product pipeline capacity.

By 1990 there will be (by one major oil company's estimation) an 18% reduction in the consumption of motor fuel. With greatly reduced market for refined product, refiners could be expected to take whatever steps are necessary to gain a larger share of the retail market. One possible move by the refiners would be to greatly increase the subsidization of marketing through direct stations in order to increase refinery runs to economic levels of operation and thereby increase their overall profitability. The fact that this trend is already underway is evident from the increased emphasis on marketing by the big oil companies

17. Q. HAVE SOME OF THE 16 REFINERS WHO WOULD BE DIVORCED FROM RETAILING SOLD BRANDED GASOLINE AT RETAIL IN THEIR (COMPANY STORES) AT LESS THAN ACTUAL COSTS ASSESSED LEASSEE DEALERS BY THESE SAME REFINERS?

A. Yes. It must be remembered that refiners control and fix their competitor's wholesale price, occupancy charges and credit card surcharges and that overhead expenses must be covered in retail prices. The refiners are failing to recover these same costs when pricing gasoline at company-operated outlets.

18. Q. ARE INDEPENDENT DEALERS AS EFFICIENT AS COMPANY-OPERATED OUTLETS?

A. Yes. Independent dealers are as efficient as company-operated outlets. Dealers have more drive to maximize customer satisfaction. They exhibit more interest in and their service to consumers is superior.

An illusion of superiority in efficiency is created by refiners' behavioral practices. A long-standing method of loading wholesale

prices charged independent dealers selling the refiners' trademarked identified products causes this illusion. The practice of refiners' company-operated outlets selling gasoline to consumers at retail prices that are less than that loaded wholesale price and/or less than that loaded wholesale price plus a property rental value equivalent to rentals charged dealers plus other operating costs of the retail outlet must be corrected to restore competition based on efficiencies.

Divorcement of the largest refiners from retailing and prohibition of such anti-competitive, dual marketing practices will restore equity and sanity as well as allow the more efficient to survive in the retail marketing of petroleum products. S.40 and H.R.1755 are intended to accomplish that objective.

19. Q. IS THERE ANY REASON WHY AN INDEPENDENT DEALER CANNOT OPERATE A HIGH-VOLUME OPERATION AS EFFICIENTLY AS THE MAJOR INTEGRATED REFINERS?

A. No. There is no reason why an independent dealer cannot operate a high-volume operation as efficiently as major integrated refiners or jobbers.

If integrated refiners continue to withhold their best high-volume locations as company-operated outlets and if they continue current marketing practices, efficiency will not determine who survives in the marketplace. The ability to transfer product to company-operated outlets by refiners at less than dealer wholesale prices, the ability to ignore property rental cost and other actual operating costs of retailing, and the ability to sustain an unlimited economic loss will destroy dealers regardless of how efficient dealers are.

Texaco's new Atlanta area self-serve retail outlets that are company operated are moving

high volumes because they are transferring product to those locations at wholesale prices that obviously are much lower than Texaco charges the dealers (see evidence submitted during Senate hearings). Texaco is also not covering in their retail prices the \$5,000.00 to \$6,000.00 monthly rental they tied to the properties that caused the eviction of dealers from those locations. That sort of practice is not efficiency. Any dealer, given the same low wholesale price and low rental cost, could be just as volume efficient and could reach just as high a volume as Texaco has by company operating these outlets. Divorcement and Open Supply will provide relief essential to preserving competition.

20. Q. NOW THAT CONTROLS HAVE BEEN LIFTED, WHAT PROTECTIONS DO INDEPENDENT DEALERS HAVE IF THERE IS A SEVERE SUPPLY CUT-OFF?

A. None! Dealer franchise agreements, lease and supply contracts, provide a refiner may be excused from performance at any time and for any reason when there is insufficient supply from a cause reasonably beyond the refiner's control. For example:

Article XII of the Shell Oil Company dealer lease reads:

EXCUSES FOR NON-PERFORMANCE. Shell shall be excused from performance of its obligations under this Agreement when and to the extent that such performance is delayed or prevented by any cause reasonably beyond Shell's control. If Shell's supply of any Product at Shell's plant is or will be insufficient, at any time or for any reason, for Shell to fill all orders which normally are or would be filled therefrom (whether from contract or non-contract purchasers), Shell may dis-

continue deliveries of such products hereunder or apportion deliveries thereof among orders received from dealer and from other purchasers, in such manner as Shell in its sole discretion, may determine.

Article V of the Chevron U.S.A. dealer lease reads:

(a) There shall be no obligation to deliver or to receive or use the products herein described when and while, and to the extent that, the receiving or using or manufacture or making deliveries in the customary manner are prevented or hindered by act of God, fire, riot, labor disturbances, accident, war or the acts of any government (whether foreign or domestic, federal, state, county or municipal) or any causes beyond the reasonable control of the party affected, whether or not similar to any of the foregoing causes. In cases of partial or total interruption or loss or shortage of transportation facilities or supplies, or shortage of products deliverable hereunder, Chevron shall have the right to pro-rate the delivery of available products among dealer and other outlets and customers of Chevron, contract ...

There is no assurance product would be prorated in case of a supply cutoff. The opportunity for refiners and for jobbers to favor their company-operated outlets is self-evident and could be fully expected. Behavioral practices of the past certainly indicates little regard would be given to equitably treat dealers in event of a severe supply cut-off.

21. Q. BASED ON PAST EXPERIENCES, WHAT DO YOU EXPECT WOULD HAPPEN TO THE INDEPENDENT DEALER WITHOUT THIS LEGISLATION IF THERE WAS ANOTHER SEVERE SHORTAGE?

- A. There would be an overnight slaughter of dealer-operated outlets. Independent dealers would face abrupt total loss of product or disproportionately larger loss than company-operated outlets would experience, and customers of dealers would not only be switched to being customers of company-operated outlets but will be required to use more fuel to reach the fewer company-operated locations that have product to sell.

History is our best teacher. Without passage of divorcement and open supply legislation the largest refiners would repeat their self-serving and selfish actions that caused Congress to enact the provisions of the Emergency Petroleum Allocation Act.

22. Q. HAS THERE BEEN A SUCCESSFUL SUIT UNDER THE EXISTING LAW CHALLENGING PREDATORY PRACTICES BY REFINERS?

- A. No! To the contrary, the courts have declared that a transfer of product from storage of a refiner, or a jobber, is not a sale but an intra-company activity that is not a violation of anti-trust laws. There are therefore no clearly stated laws that afford protection of competition and small business dealers in the marketing of petroleum products from the structural and behavioral activities sought to be corrected. The only way to effectively prohibit such conduct so as to preserve competition and small business opportunities in the petroleum industry is by enactment.

Even if there is implied prohibition against such behavioral activities of refiners in the anti-trust laws and/or in the FTC Act, relief is not reachable. The recent actions against the refiners which FTC dropped is evidence that small business does not have any chance of suc-

cess under present laws if, in fact, such laws are applicable.

23. Q. WHY IS THE OPEN SUPPLY PROVISION NECESSARY?

The open supply provision of S.40 and H.R.1755 is necessary to provide a competitive climate that has long been missing among the nation's dealers who purchase refiner product for resale under trademarks. There has been little to no downward pressure on refiner, and jobber, wholesale prices charged dealers for branded products purchased for resale.

Artificially higher wholesale prices have historically been charged branded dealers as a consequence. Yet, the same product has been sold by the same refiners to other than their branded dealers at substantially lower prices than are justified by reasonable charges for trademark, advertising and credit card processing costs associated with branded product sales. It was competition from other sources of supply that has resulted in lower prices (at wholesale) that has caused the unreal and unjustified differences in retail product prices.

Clearly establishing that dealers, and jobbers, are free (some say dealers already have that right -- there is evidence that supports the need) to purchase the same brand from another supplier or to purchase, store, and sell another product on the premises will provide downward pressure on wholesale prices to branded dealers. Since the largest portion of all products purchased by consumers is branded products, the public's potential benefit is too great to estimate.

An open supply provision will further the original intent of the antitrust law ... to prohibit tying arrangements or exclusive deal

ing agreements unless suppliers meet competition.

An open supply provision will permit the dealer whose supplier has priced him out of the competition to substitute another product with appropriate notice to consumers.

An open supply provision will unlock the invisible but effective door that has been shut too long that keeps other suppliers from calling on branded dealers, which suppliers may offer an equally good product at substantially lower prices.

Yes, the open supply and divorcement provisions are necessary to effectively ensure maximum benefits flow to consumers in the normal and usual manner that should and must exist under an unencumbered free enterprise marketing system upon which this nation has prospered.

24. Q. WHAT IS THE TRUTH ABOUT THE NUMBER OF COMPANY STORE OUTLETS FOR THE SIXTEEN LARGEST REFINERS?

- A. Even though the number of company store outlets for the sixteen largest refiners decreased 235 from 1972 through 1978, when adjusted for the increased average monthly volume sold by the remaining company stores, the effect was the same as building 6,076 new company store outlets.

The latest statistics show growth (1977-1982) at 11.7%. During the same period the number of leasee dealers decreased 34.2%.

The additional volume of products sold by the refiners could not have been sold without lowering of the price and underselling dealers as they did while holding the dealers wholesale prices at a level that did not permit the dealer to compete with them. The open supply

provision coupled with the prohibition for these refiners to operate retail outlets will restore equity and fairness in the marketing of gasoline and preserve competition for the benefit to consumers.

25. Q. ARE DEALERS' REAL AIM TO DIVORCE JOBBERS FROM RETAILING?

- A. No! Though divorcement of jobbers is a clean cut way to correct abusive anticompetitive marketing practices of jobbers, the Service Station Dealers of America are only seeking relief that will preserve competition in the marketing of gasoline. Divorcement and open supply may solve and/or correct the anticompetitive marketing practices which some jobbers are engaged in.

The Congress will decide, not the Service Station Dealers of America, if at some point in the future jobbers should be divorced from retailing because they have not corrected their abusive practices and because no other acceptable solution has been found.

Jobbers have publicly admitted that there are abuses. Jobbers have publicly offered alternative proposals to correct those abuses. Jobbers know that they are destroying dealers who must purchase products from them and must pay whatever price they choose to charge. Open supply could provide the appropriate competitive element that would cause jobbers to cease engaging in anticompetitive marketing practices and thereby remove any possibility of future legislation of any sort.

26. Q. WHAT AUTHORITIES HAVE EXAMINED RETAIL MARKETING PRACTICES AND HAVE EXPRESSED FINDINGS THAT SUPPORT THE CONCEPT TO CORRECT THESE ANTI-COMPETITIVE PRACTICES THAT DENY DEALERS THE BASIC FAIRNESS INTENDED BY THE PROPOSED DIVORCEMENT AND OPEN SUPPLY LEGISLATION?

A. Partial answer includes:

- (1) "FTC Report on Anti-competitive Practices In The Marketing of Gasoline" (1965 Hearings), June 30, 1967;
- (2) "House Small Business Committee on Problems of Small Retail Petroleum Marketers," October 20, 1976;
- (3) "Petroleum Marketing Practices Act of 1978," Title III, Requirements for Study and Intended emergency relief;
- (4) D.O.E., Office of Competition's Trend in Company Stores, December 1979;
- (5) "House Small Business Subcommittee on Anti-trust and Restraint of Trade Activities Affecting Small Business," transcript of 8 hearings on Gasoline Marketing Practices, 1979;
- (6) House Small Business Committee Report 96-1068, June 3, 1980, filed after hearings and investigation of petroleum industry practices by Subcommittee on Energy, Environment, Safety and Research;
- (7) "Big Oil: A Citizen's Factbook on The Major Oil Companies," Center for Science In The Public Interest, 1973; 1974;
- (8) Allvine/Houston/Phillips, "The Case for Legislative Relief From The Impending Destruction Of Small Business And Competition In The Gasoline Industry." Georgia Association of Petroleum Retailers, January 22, 1980;
- (9) D.O.E., Office of Competition, Part I, Title III Report, May 1980 and J.W. Wilson & Associates, Inc. Economic Counsel, Washington, D.C., "Report On Part I The State Of Competition in Gasoline Marketing; The Effect of Refiner Operations at Retail," September, 1980; and transcript of all related Hearings.
- (10) Small Business Administration's contracted Final Report from the Institute of Public Administration, Washington, D.C., "An Analysis of The Department of Energy's Fuel Allocation Plan and Related Policies," particularly pages 110-117 and especially page 115, 3rd paragraph and 1st sentence on page 116, June 1980: recom-

mending divorcement of refiners and jobbers from retailing.

(11) Testimony on legislation by the National Small Business Association;

(12) Testimony on legislation by the National Federation of Independent Business;

(13) White House Conference on Small Business, 1980;

(14) American Petroleum Institute, testimony by Mr. Paul D. Collier before U.S. Senator Howard Metzenbaum's Subcommittee, openly admitted the retail marketing system as it was designed by refiners and as it exists today is a disadvantage to the independent branded dealer stations. The admission by the representative of API is significant in that it succinctly identifies the problem. The problem is that independent service station dealers are being squeezed out of business.

(15) The Office of Advocacy, Small Business Administration, in testimony on the 1980 divorcement/anti-competitive pricing legislation said: "If we choose at this moment between no legislation and 'imfect' legislation which does not have the equally enthusiastic support of all small business elements in this industry, it is far more important to have even the 'imperfect' legislation. We can all work to perfect it as soon as Congress reconvenes. But the longer we go without even imperfect legislation, the fewer small businesses there will be to participate in the perfecting process."

(16) Federal Trade Commission -- According to The Oil Daily (November 4, 1980): Complaint filed against eight refiners (Exxon, Texaco, Gulf, Mobil, Standard Oil of California, Standard Oil of Indiana, Arco, Shell) November, 1980 charges the refiners have individually and collectively:

"have restrained trade and maintained and reinforced a non-competitive market structure in the refining of crude oil into petroleum products.

"To this end, respondents (the oil companies) engaged in a common course of conduct that restrained trade and commerce at every functional level of the petroleum industry."

The Oil Daily further said the complaint charged that the companies violated antitrust laws by using their leverage over refining and marketing sectors of the industry ... and that it is expected resolutions of the complaint will take into the 1990's.

27. Q. IN SUMMARY, WHAT IS THE KEY ISSUE THAT STANDING ALONE JUSTIFIES PASSAGE?

A. In Summary, Refiners engaged in retailing are "predators" and they are unnatural and unfair "competitors" because the refiners:

1. Control and fix the wholesale prices paid by their competitors;
2. Control available sources of supply to competitors;
3. Fix occupancy cost of outlets operated by competitors;
4. Require unproductive operating hours costs that competitors must bear;
5. Assess other operating demands that increases their competitor's costs; and

Refiners then fail to recover those same costs when pricing gasoline on retail pumps at their company-operated outlets.

Prepared and Published By:

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Executive Director,
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(202 / 393-6868 -- 404 / 296-0305)

March 1984

Go For Fairness

"IT IS DIFFICULT TO THINK OF LIFE
IN AMERICA WITHOUT THINKING OF THE
TENS OF THOUSANDS OF SERVICE
STATIONS THAT DOT OUR HIGHWAYS AND
PLAY SUCH AN IMPORTANT ROLE IN THE
LIVES OF OUR CITIES AND TOWNS --
BOTH ECONOMICALLY AND AS A VITAL
PART OF COMMUNITY LIFE."

Ronald Reagan, President
The White House
May 18, 1981

Senator MATHIAS. Mr. Price.

STATEMENT OF ARTHUR E. PRICE

Mr. PRICE. Thank you, Mr. Chairman.

I am Arthur Price, administrator of inspection and testing for the comptroller of the treasury, State of Maryland. On behalf of Comptroller Goldstein, we would like to thank you for this opportunity to express our thoughts and our experience relative to service station divorcement, as provided for by S. 40.

Maryland enacted similar legislation in 1974. However, due to challenges up to and including the U.S. Supreme Court, implementation did not occur until June of 1979.

In the interest of time, I will leave with the committee copies of Maryland Comptroller Goldstein's testimony before a committee of the U.S. House of Representatives on March 31, 1981, regarding this same matter that was contained then in H.R. 1362. We are also providing to the committee my testimony of October 21, 1981 before the Judiciary Committee, regarding S. 326 and the subsequent written questions and answers to Senator Thurmond that provided statistics and facts relative to Maryland's experience with divorcement.

As you know, S. 326 received favorable consideration from the Judiciary Committee, I believe, during the last Congress.

We sincerely believe divorcement in Maryland has greatly reduced the demise of the independent service station operator, while significantly benefiting the consumer. Permit me to illustrate.

In Comptroller Goldstein's previously cited testimony, evidence was provided that that service station population nationally had declined by 20 percent—33,900 units—between January 1979 and March 1981. In Maryland for that same period, the loss of outlets was only 5.6 percent. Since that time, here is what has happened in Maryland versus the national picture.

In calendar year 1981, Maryland experienced a loss of 4.3 percent; the national number was 4.4 percent. In 1982, Maryland had a loss of 3 percent, and the national average was nearly 5 percent. And for the year ending January 1, 1984, we experienced a 3.4-percent loss against the nationally projected number of 4.8.

Percentagewise, our loss of service stations is one-third less than the national average. Because salary operations are not permitted in Maryland, we believe the conversion to gas-only-type stations has been retarded, thereby retaining more service stations with service bays to perform emergency and other service-related functions. Divorcement has certainly brought stability to the marketplace. A refiner can no longer eject a dealer on some whim. Refiners can only operate a station for one of three specific reasons, and then only for the limited period of time permitted by the State. This, we believe, has prevented dealer expulsions in large numbers, and any time you afford the dealer more security, you give him a reason to invest in more and better equipment with which he can better serve the public.

Consumers in Maryland have benefited from lower prices. Let me illustrate how that occurred. Prior to divorcement in Maryland, BP operated 82 stations with salaried personnel. After divorcement, these stations were essentially operated by 82 individual dealers, creating 81 new additional actors in the marketplace, all vying for your business.

What happened? The only element a dealer can add to in your cost of gasoline is his profit or margin. Taxes are fixed by governments and tankwagon costs determined by the supplier. The independent and neutral Lundberg Letter continues to report month after month lower dealer margins in Baltimore than in other east coast cities. The most recent National Petroleum News Annual Fact Book, 1983 issue, pages 88 and 89, contain among other things the fact that average dealer margins for calendar year 1982, they report upon 52 cities, and only 3 are lower than Baltimore. This publication reflects the average dealer margin of 2 cents per gallon less in Baltimore than in Boston, MA. This 2-cent savings on the 2 billion gallons consumed by the Maryland consumer translates into an annual savings of more than \$40 million.

Let me assure the committee that no one has left the State of Maryland; the same companies paying taxes to us prior to divorcement are still filing monthly reports and paying taxes to us today. If a company desires to realign its marketing strategies, it will be done with or without divorcement. This is certainly illustrated by Texaco's withdrawal from portions of New York State, Crown's

sale of all outlets on Long Island to Amarada-Hess, and Exxon's withdrawal from Ohio, Vermont, and New Hampshire. None of these States has a divorce law. Divorcement is healthy.

One final comment. Comptroller Goldstein has testified before, and we once again now urge the committee not to exclude any producer refiner from the provisions of S. 40. Crown Central Petroleum, doing business in 8 States, Amarada-Hess big in the Northeast, Kerr-McGee with over 1,800 outlets doing business in 18 States—and there are others—all of these, I believe, would be excluded because of the small refiner definition. However, they are big factors in their respective local markets.

If, after careful analysis, the committee feels it is still desirable from a national standpoint to exclude small producers and refiners from divorce, we urge you to include appropriate provisions in S. 40 so as not to preempt stricter provisions of similar State statutes.

Thank you, Senator.

Senator MATHIAS. Thank you very much.

You coasted in right under the red light.

Mr. Molnar.

STATEMENT OF RUDY MOLNAR

Mr. MOLNAR. Thank you, Mr. Chairman, for the opportunity to speak before the committee today.

My name is Rudy Molnar. I am from Pittsburgh, PA. I have been an independent service station dealer for 24 years.

I was president of the State Association for 10 years. I have lived through two gasoline shortages. I have seen many changes in the gasoline industry, and in 24 years, I will say the last 2 years have been the roughest. This, in modern terms, is called the pits.

The reason given by the oil companies for Pennsylvania losing over 50 percent of its stations is that the economy has changed. The industry has adjusted itself to different lifestyles. We do not feel this is so. Our State legislature does not agree that this is the only reason, also.

Over the past 2 years, the State senate has passed total retail divorce by an overwhelming margin. The State house has passed a different version of divorce. Presently, the bill is in a House-Senate Conference Committee, in which a compromise bill hopefully will be reported. Apparently, the legislators believed there were other factors at work besides economic change in the gasoline marketplace that were forcing dealers out of the market.

In 1982, as part of the legislative inquiry as to dealer problems, the Governor's Energy Council, the GEC, an agency of State government, made an indepth study of Pennsylvania's gasoline market. According to the study's conclusion, " * * * the investigation revealed a number of marketing practices which work to the disadvantage of the independent dealers." These practices were documented by the GEC. They included proof of exorbitant rent increases, situations in which refiners were selling the product through company operations in competition with their own dealers at or below the wholesale cost offered to the dealer, and the arbitrary use of price zones.

In days of hearings, we documented actual case of refiners using tactics which circumvented the legislation passed in the seventies to protect dealers, the PMPA. The GEC report concluded that the review of Federal and State laws and court interpretations of PMPA showed, " * * * that the laws provide little or no legislative remedies for the abuses cited." That is the frustration we as small businessmen face. It is very difficult to go into court and to take 5 years as an independent station, to take an oil company to court, at the cost of anywhere between \$35,000 and \$50,000 a case. The oil companies know this, and this is how they break our backs.

This is why we are asking you for help today. We all know divorcement has passed in some form in several States. We also know that the predictable attack of oil companies of divorcement causes prices to rise. It is important to note that in comparison of the Maryland and Pennsylvania gasoline market for a 2½-year period, the GEC study reported that available evidence provides no clear answer as to how this legislation affects consumer prices, but estimates of prices weighed by type of sale in Baltimore and Philadelphia suggest that consumers on the whole are not affected by divorcement legislation.

But the consumer will be affected if service station dealers are removed as a force in the marketplace. In this era of rapid oil mergers, the retail end of the oil chain may be the last vestige of competition possible to preserve. But time is running out.

We in Pennsylvania urge the enactment of divorcement on a Federal level. We would be pleased to share our experiences with committee members and staff. Anything we have documented, I would be very happy to give you upon request.

It is through your actions that we hope to survive as small business people. Remember—when oil companies get in trouble, they merge; when we, the dealers, get in trouble, whether it be a loophole in PMPA, or just unfair marketing practices, we cannot merge. We just go out of business—just one more statistic on big oil's record of continuous elimination of the independent service station dealer from the marketplace.

United States Steel, in its continuing effort to thwart the Japanese marketplace on steel, is continuing its efforts to have laws put in that would protect them from the unfair practices of the Japanese marketplace in steel. We feel that they have every right to do so. The oil companies own our properties. United States Steel owns their own. They can buy their products anywhere they want. We cannot. So we are even in a worse position. That is why it is very frustrating to see United States Steel's acquisition of Marathon, testifying against divorcement, when their parent company asked the same thing we ask here in a different form.

Thank you for your time.

Senator MATHIAS. Thank you very much.

[The following was received for the record:]

OFFICE: (215) 499-6400
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Pennsylvania and Delaware Service Station Dealers Association

3846 RIDGE PIKE
COLLEGEVILLE, PA. 19426

TESTIMONY OF RUDY MOLNAR, VICE PRESIDENT
FOR GOVERNMENTAL AFFAIRS, PENNSYLVANIA
AND DELAWARE SERVICE STATION DEALERS ASSOCI-
ATION, BEFORE THE SENATE JUDICIARY COMMITTEE
MARCH 14, 1984.

Thank you, Mr. Chairman, for the opportunity to speak before the committee today.

I have been an independent service station dealer in the city of Pittsburgh for over twenty years, and was President of the state service station dealers association for nearly ten. I have lived through two gasoline shortages. I have seen many changes in the gasoline industry.

But I have never seen anything as drastic as the rapid closing of independent service stations in the state of Pennsylvania over the past three years.

A reason given by the oil companies for Pennsylvania losing over 50% of its stations since 1978 is that the economy has changed, the industry has adjusted itself to different lifestyles.

Our state legislature does not agree that this is the only reason the number of dealers is dwindling. Over the past year and a half, the state Senate passed total retail divorcement by an overwhelming margin. The state House has passed a different version of the same concept. Presently the bill is in a House - Senate Conference Committee in which a compromise bill hopefully will be reported. Apparently the legislators believed there were other factors at work besides economic change in the gasoline marketplace that was forcing dealers out of the market.

In 1982, as part of the legislative inquiry as to dealer problems, the Governor's Energy Council, an agency of state government, made an indepth study of Pennsylvania's gasoline market. According to the study's conclusion: "... the investigation revealed a number of marketing practices which work to the disadvantage of the independent dealers." These practices were documented by the GEC. They included proof of exorbitant rent increases, situations in which refiners were selling the product through company operations

in competition with their own dealers at or below the wholesale cost offered to the dealer, and the arbitrary use of price zones.

In days of hearings, we documented actual case of refiners using tactics which circumvented the legislation passed in the seventies to protect dealers. But every month there were fewer dealers in business to use as examples.

The GEC report concluded that the review of federal and state laws, and court interpretations of PMPA, showed, "that they (the laws) provide little or not legislative remedies for the abuses cited." That is the frustration we as small businessmen face. That is why we are asking you for help today.

We all know divorcement has passed in some form in several states. We also know the predictable attack of oil companies that divorcement causes prices to rise. It is important to note that in comparison of the Maryland and Pennsylvania gasoline market for a two and one half year period, the GEC study reported that :

Available evidence provides no clear answer as to how this legislation (divorcement) affects consumer prices, but estimates of prices weighed by type of sale in Baltimore and Philadelphia . . . suggest that consumers on the whole are not affected by divorcement legislation.

But the consumer will be affected if service station dealers are removed as a force in the marketplace. In this era of rapid oil mergers, the retail end of the oil chain may be the last vestage of competition possible to preserve. But time is running out.

We in Pennsylvania urge the enactment of divorcement on a federal level. We would be pleased to share our experiences with committee members and staff.

It is through your actions that we can hope to survive as small business-people.

Senator MATHIAS. Mr. Jackson.

STATEMENT OF CONRAD JACKSON

Mr. JACKSON. Mr. Chairman, Conrad Jackson is my name, from Mobile, AL. What I have to offer to this committee today is what we refer to as "Weekend Number 3," Saturday, December 2, 1978, from 10 p.m. until 11 p.m., by the National Broadcasting Co., Inc.

This document covers so much, I do not have the time allotted me today to read it to you or discuss it. However, there are enough copies of this document available that we can make available to you that can explain to you how the major oil companies go about getting rid of you when you are put on the hit list.

Senator MATHIAS. I can assure you, Mr. Jackson, the full statement will be included in the record. That will be printed and distributed to every member of the committee here and be available for the public, so that your full statement will be a part of this record.

Mr. JACKSON. Good.

I went with Gulf Oil Corp. in 1958. Everything went fine until the shortage came along in the latter part of 1974-75, whenever it was, and the base periods were installed, back in 1972-73. My customers, the customers I had been serving all these years, would call me for product. The tanks at Gulf Oil Corp. alone, the lids would be floating on them, running over. But unless they were on the printout sheet, they were not eligible to get any product. So as a result of this, after my customers became beligerant with me, I went to the company and said, "Something has got to be done." Maybe they did not buy any in 1972 or 1973; maybe they did not need it. But they need it today, and we have got to have product for them. So I was asked the question if I could buy product on the outside. My answer to that question was, "Yes," I could buy product.

They told me to be their guest. I in turn asked them to put it on paper and sign it; give it to me, and I would be glad to go and pick a product anywhere and take it to my customers. They would not put anything on paper.

However, I did have the permission to go and get it and take care of my accounts. I went on through this until the regulations or what have you were eliminated, and then product was plentiful. Then they came back to me, and they said, "Now that we have plenty of product, we want to push Gulf products."

I said, "Fine. That's great. I'll push Gulf products."

So they wanted me to eliminate the people who had let me have product during the shortage 100 percent, and move their product. I told them I could not do it. I could not bite the hands that had fed me all these years.

So we arrived at a 60/40 agreement: 60 percent Gulf, 40 percent outside. Then I made it my business to stay within those bounds. Yet about 3 months prior to June 8, 1978, they approached me with a mutual consent of dissolution, termination, or what have you. I immediately informed them that I could not sign anything without talking to my attorney, and they left. That was the way it was. On June 8, I was terminated as a Gulf distributor or commission deliv-

ery, whatever you want to call it. In 1978, that eliminated me as a businessman in Mobile, AL. I tried it for a few years and channelled everything back into it that I had accumulated, and today I am padding the concrete, just like I did when I started years ago.

That is all I have, sir.

Senator MATHIAS. Thank you very much, Mr. Jackson.

[The following was received for the record:]

WEEKEND #3SATURDAY, DECEMBER 2, 197810:00 PM - 11:00 PM

National Broadcasting Company, Inc.

MAN

Now comes a new development. In recent weeks, the Canadian Government announced the discovery in Northern Alberta of one trillion barrels of heavy crude oil in place, one trillion barrels, that means that Canada's heavy crude contains more oil than Saudi Arabia, Iran and all the rest of the Middle East together.

COMM. MESSAGE: SUBARU

COMM. MESSAGE: SELSEN BLUE SHAMPOO & SELENE

MUSIC

LE

Three years ago, Weekend reported that major oil companies were beginning to squeeze out their own dealers -- small businessmen operating under a franchise.

Some companies were squeezing harder than others.

Consider this a progress report. It is that because there was progress.

The plan worked.

- 12-

LE

The squeezer -- Gulf Oil.

MAN

Mr. Ron Dean, for example, was a Southern California District Manager, made out a list that says "targets for mutuals."

LE

What you're saying is that in 1975, Gulf Oil executives had in their hands an "enemy's list" of their own dealers they wanted to put out of business?

MAN

That is correct.

MAN

The Gulf representatives come to my station in Buellton and told me they wanted the station back they wanted to make it a SELF-SERV, how fast could I get out?

MAN

I didn't want to get out I just kept on thinking this fellow on the great white charger would come in one day and kind of save us.

MAN

Yeah, I was supposed to be in the cream of the crop after we got rid of all the others, ^{why} when we was

MAN

really going to run with the top dealers. I was told many times that the station was mine for as long as I wanted it...and now I find myself going out with the rest of them.

LE

This is a familiar scene to most Americans, except that it's about to disappear in California. Gulf is virtually withdrawing its brand name from the west coast retail market. They will still sell gas in California but it won't be called Gulf. This is not a story about Gulf's decision to change its marketing practices, that is Gulf's business, this is a story about the way Gulf treated its own dealers wiping out more than a thousand of them in Southern California in just 5 years using its considerable corporate power to put out of business the same small businessman it put into business.

LE

Remember the "full service" filling station? Fill your tank? Check your oil? Change your tires? Fix your battery? Whatever you need, sir.

For twenty years the oil companies built as many as possible to pump as much crude oil as possible, because that's how big profits were made.

LE

But there were too many filling stations, and they were being undercut by the independents.

So the company-owned, dealer-operated, "full service" filling station began to die out, or be pushed out. And not just at Gulf.

But at Gulf, especially on the west coast, that push was more dramatic.

So were the results.

In 1972, there were more than a thousand dealer-operated Gulf stations in that area. Now there are fewer than sixty.

You can still buy Gulf gasoline. ECONOMY is Gulf. GO-LO is Gulf.

They are secondary brands. That means Gulf owns and operates these stations.

Under the dealer system, the stations were run by a businessman who had the franchise.

Gulf believes the company-run stations are a better deal.

At least for Gulf.

They sell you gas only. You can pump it yourself. This is no-frills service.

Independent marketers, like Thrifty, were offering "gas only - no frills" long before it

LE

occurred to the big companies.

Gulf and the other majors were accustomed to ~~pk~~ competing with each other with ad campaigns, giveaways~~x~~.

The independents had price wars.

Then, the majors responded with their own price wars...and drove many independents out of business.

In 1973, OPEC cut off the oil.

The majors began to copy the independents especially Gulf.

Gulf decided selling "gas only" was more profitable.

Gulf decided running the stations itself was more profitable.

If the dealers were in the way, perhaps a way could be found to move them out.

Perhaps several ways could be found.

CHARLES KENDALL

I believe it was in May of 1975...

LE

Charles Kendall -- a former Gulf sales representative -- began keeping documents and tapes. He was afraid his company had broken the law and afraid he would be held criminally liable.

LE

He recalls a meeting about the dealers between company salesmen and Gulf's #2 West Coast executive.

KENDALL

He said that he had a list of stations that they wanted to get out before the end of 1975 and he was going to pass it around to let each of the TBA, the TBA center managers see the list. And Mr. Curt Williams had some notes in front of him as I have here and he looked at 'em and said Bob I don't think we should pass this around someone might refer to it as the "enemies list."

LE

This is part of the list the Gulf executive~~x~~ was~~x~~ afraid someone would call an "enemies list."

The numbers represent stations where Kendall and other Gulf reps were supposed to persuade dealers to sign agreements of mutual consent to end their contracts with Gulf -- agreements to be put out of business, really.

Numbers with an asterisk, said Kendall, meant go slow, this dealer might cause trouble.

Numbers with lines drawn through them of checkmarks represented stations already terminated. They were gone.

LE

Number 1754.

Number 1754 was a Gulf station on the outskirts of San Bernadino.

Number 1754 was also Red Fair, the dealer who ran the station.

Fair held on to his station until last summer.

He says he was forced out by ~~Santa~~ Gulf --though Gulf had never even told him he was a target.

FAIR

As a matter of fact, I wasn't aware of it 'til about a month, maybe a month and a half beforexx I was put out of the service station...but it did, it did answer a lot of questions some some of the things that had been going on.

LE

The "things going on," according to Kendall, included a statement that the way to put dealers out of business was to put them into debt.

The dealers buy tires batteries and accessories -- called TBA -- from Gulf.

The idea, said Kendall, was to get the dealers by persuasion or threat, to buy more TAB than they could afford.

Kendall says he ~~was~~ asked that same West Coast

LE

executive about this at a meeting in May of 1975x.

KENDALL

Mr. Byrnes' remarks was well, Charlie, can you ~~xx~~ tell me of a better way of getting the dealers out than to load them down with their tires batteries accessories and get them so loaded down that they can't make their monthly payments?

LE

Art Wallbaum was one of the victims'--over-stocked with tires he could not sell.

WALLBAUM

I probably had in excess of 7 hundred at one time, I had tires everywhere, in fact we had 'em ~~x~~ in the bay at times and we couldn't even work in the bays because we had tires all over.

LE

When

Danny Davis was forced out at Gulf, he went to Mobil. Gulf refused to buy back his stock. He took it with him.

X DAVIS

Well, I say I brought with me approximately four thousand dollars in merchandise and I've been selling that merchandise at half-price in order to try and retrieve ~~xx~~ some of my money, trying to sell

DAVIS

something like that to the public is almost an impossibility and I'd say I'd lost a couple of thousand dollars on those products.

LE

Kendall said that during the gas shortage of 1974, a Gulf executive told the sales reps to threaten the dealers, TBA went with the gas, Period.

KENDALL

Mr. Meyer told the marketers that any dealer that did not wish to go along with the ~~TBA~~ TBA program you tell that dealer that we at Gulf can sell all the gasoline we can get and we'd like to have the stations back as an ECONOMY operation and he beats pounded his fists on that table while making those remarks that they bought tires or you tell them they don't get gasoline.'

LE

A Gulf executive walks into a sales meeting says tell the dealers if they don't buy the tires they don't get the gasoline, were any dealers told that?

KENDALL

Yes, they were, in my presence, approximately twenty five.

LE

Just that?

MAN

Told that in those exact words.

MAN

Yes, during the so-called crunch I was told that if I didn't buy tires no gas, and I did buy tires, I carried lots of tires and I never did run, run out of gas.

MAN

I didn't see fit to buy at that time, I was stocking over 2 hundred at the time, and consequently I run out of gas several times, once for 17 days out of the month they just cut me off, wouldn't deliver any to me at all.

LE

The dealers and Kendall ~~was~~ claim the method was to send the company-man to the station get the dealer off to one side and discuss his tire program, of if the time seemed right persuade him to give up' and get out.

KENDALL

Well the approach was always let's go somewhere and have coffee, and we got away from the station, and at that time they would say well we have a tire sale

KENDALL

and we have these goals to meet and your quota will be 100 tires and this was forced upon you by them.

MAN

If you don't want to go along with the program, why don't we shake hands and part friends and let's let Gulf have it back and let's go to ECONOMY oil which is a company operation.

MAN

You take the dealer out behind the station or down the street someplace away from everybody and it was just your word against his.

LE

Gordon XCurTISS was also a Gulf salesman for nearly fifteen years.

He says he knew what the company was doing, and he says he knew why — because they talked about it.

CURTISS

Once a year they'd call in all the personnel for a meeting with the company's attorneys, which would tell you of court cases and ~~the~~ the legality of things that had happened, what you could and could not legally do, and if you should say something that would get you into trouble or be sued by a dealer that you would go to court by yourself and they would not

CURTISS

furnish legal representation to you, that they would not back you up in things that you were trying to do in the course of your duty...and yet they would tell you things to do but yet if you got caught they weren't, they weren't condoned by the company.

LE

Other ~~dealers~~ dealers were forced to quite when Gulf changed its policy about gasoline delivery.

Before 1974, dealers paid only for the amount of gas they sold to customers at the pumps.

They paid a small deposit for the gasoline in the ground.

Suddenly, Gulf demanded payment in advance -- plus a large deposit.

The government stopped it, but not, according to Rex Kerr, in time.

Kerr says Gulf pushed him out of both his stations.

A jury agreed, and awarded Rex Kerr 78 thousand dollars.

Kerr says one of his stations was lost just because of the new delivery policy.

Kerr said business was just fine -- the location

LE

was excellent.

The station was in Santa Maria, on a major highway, next to a Holiday INN.

But Gulf won, he lost...and that good location is now just another abandoned filling station.

KERR

Yeah, I was buying my gas as I sold it. Then they told me to buy my gasoline in advance, this required 8 thousand dollars per station -- I had to buy a total of 16 thousand dollars worth of gas. Then they increased my deposit 16 thousand dollars and the next thing I knew I was obligated to a 30 or thirty one thousand dollars in gasoline and deposits, which I only had 2 thousand or 3 thousand dollars in deposits to begin, and I started experiencing terrific financial problems, so I liquidated one of my stations.

LE

Then, says Kerr, Gulf began to squeeze him out of his other station in Buellton, 30 miles south.

KERR

I would get the stuff in writing from Gulf Oil Company telling me to, to lower my prices, to increase my hours, to, in the meantime they were

KERR

raising my price right along. One time I was even with competition, they said it would be better if I lowered a couple of cents below them. And I said it's not practical, financially, I said the demands there, if I would like to have more of a margin to operate on and they says you're going to lower your price, ~~xx~~ we're going to be out. I think it was on a Sunday morning, and your prices better be down two cents lower than your competition... and they came in Sunday morning, and my prices were down ~~km~~ two cents.

LE

Even the court decided Gulf had gone too far, but though Kerr got damages, he had no more stations. He had fought giving up the second station.

It was his investment, his business.

And finally, his loss.

KERR

They says, well, as quick as you can we'd like for you to piack up yður stuff and get out. And I said, you know how could I get, could they buy back some of this stuff, like some of my tires batteries and accessories and the gasoline in the ground I own?

KERR

and they says, no, it would be best if you took all that with you. And I said, well what about the gas, how am I going to get it out, and you know four five thousand gallons of gas? They said well you'll have to get some barrels and fill them up and take them out, you know get the gasoline out of there if you want it, if not you just leave it.

LE

This Go-Lo station next to the San Diego Freeway used to be a Gulf station and used to belong to Bob Lee, who never knew what hit him until after he left.

Lee says Gulf insisted he stay open 24 hours a day.

Now that he's out of that business he runs a tire store.

LEE

I had originally signed a 24 hours lease, which originally, in those years, was good in the days when gasoline was 29 cents a gallon, you know 24 cents a gallon. But as the gas crunch and the increase in prices, then our business just absolutely went completely down, there was no, in our business anymore.

LEE

I asked for an 18 hour lease and they said no, it's 24 hours or nothing.

LE

Gulf insisted Bob Lee keep his station open 24 hours a day so as to sell more gas. Gulf profit@d Bob Lee did not. Between midnight and six in the morning he could not ~~xxx~~ sell enough gas even to make his expenses, in fact he says he began to lose a thousand dollars a month. Gulf does understand this now that Bob Lee is gone and Gulf operates the station it is closed from midnight until 7 in the morning.

LE

A Gulf station converted to Go-Lo or ECONOMY IS STILL Gulf...except that it's in direct competition with the Gulf franchise dealers.

MAN

I have one less than a mile, ~~x~~ one away and one about a mile and a half the other way selling ~~xx~~ for six seven eight cents cheaper than I can possibly sell for.

LE

Gulf~~s~~ says it gave its dealers a chance at their own branded stations.

- 27 -

LE

But that meant no Gulf advertising, no Gulf credit cards, and new rents so high it was almost impossible to afford them.

MAN

They have offered their dealers a new lease program and which rental would have taken me from 336 dollars a month to over 22 hundred dollars a month.

MAN

These were awards calling for an elite club sort of a ten grand club.

MAN

This one is is president's citation.

LE

So, in the end, it ~~didn't~~ ^{didn't} matter how good you were, or how good business was.

You were a dealer.

And Gulf no longer needed dealers.

MAN

Two of them were "dealer of the month" awards where I outsold everyone.

~~That~~ This one is a yearly award for "excellence as a dealer," that was in '75. Then I got the bronze one in '76, and this is my pride and joy it's a gold one for '77.

MAN

He asked one of the company reps, I thi nk it was last January, he asked him what was really going to happen. It was to the point where we were all so nervous we hesitated to invest any more money into it or anything else. And he said you dont have to worry anymore you can make all the buys you want because we've gotten rid of the "dead wood" and now we're, we figure we've got the cream of the crop, we're going to take them and run with them. So we kind of felt good again. And then the following month they dropped the axe.

LE

Gulf would not provide any of its executives ^{did} to be interviewed for this program, but ~~the~~ degree to answer some questions in a letter.

This is the letter. It is sigged Gerald Bradley, Public Affairs Department, Houston, Texas.

Gulf denies it ever pressured any dealer to leave his station so Gulf could operate it.

Of Charles Kendall -p- Gulf says he is a disgruntled employee whose statements are either untrue or misleading.

Of the "targets" list -- Gulf says "targets" was an unfortunate choice of words on Gulf's part,

LE

but denies it was a hit list.

And finally, Gulf says it is operating to benefit the consumer because says Gulf the more it can cut its costs, the more the consumer benefits.

MUSIC

COMM. MESSAGE: ASPIRIN & SUCRETS

COMM. MESSAGE: MASTER CHARGE CREDIT CARDS

STATION MESSAGE: LITTLE HOUSE ON THE PRAIRIE
SUDDENLY LOVE

MUSIC

LD

One of the problems with human frailty is it seems to bother everyone else more than it bothers you, a fact discovered anew by our participatory social mores editor, Mr. Hipp

ANIMATION: MR. HIPPI

ANNOUNCER

Artificial insemination, it allows women to bear children without physical contact with ^{men,} ~~themselves~~ next on Weekend.

STATION MESSAGE: BOB HOPE OHIO JUBILEE

STATION MESSAGE: CENTENNIAL

STATION BREAK

Senator MATHIAS. Mr. Milen?

STATEMENT OF BRUCE MILEN

Mr. MILEN. Thank you, Mr. Chairman.

My name is Bruce Milen. I am speaking to you today on behalf of the International Carwash Association/National Carwash Council, which represents over 20,000 carwash operators across the country.

ICA/NCC is the official voice of the independent carwash operator. Most of our members are small businessmen who have been serving their communities for years. Many sell gasoline at their carwash locations.

Many independent carwash operators face a special threat from the unfair competition of the huge oil companies that also operate retail gasoline stations and along with them, carwashes. We are grateful for this opportunity to explain why swift passage of Senate bill 40 is so important to our industry.

In this past year, I have been receiving many phone calls and letters from carwash operators, pleading for help from the ICA/NCC. They are literally being run out of business by the major oil companies. Oil companies are giving away a carwash with a fill-up of self-serve gasoline. In many cases, the price of the self-serve gas is less than what the independent carwash or gas station pays wholesale.

The rising number of refiner-dealers is of special importance to independent carwashes. In many instances, refiner-dealers take over operation of existing facilities and eliminate full-service operations. Often, they convert garage bays into rollover-type or tunnel carwash facilities. Then they offer a free wash with a fill-up. This price-cutting practice is an absolute disaster for independent carwashes.

Please do understand us, Mr. Chairman. We are not against competition; we welcome it. We do not want to stop retail gas dealers from washing cars. As I have already mentioned, some of us combine retail gas and carwash operations. But the competition we are facing from oil refiners is clearly unfair.

Because these energy corporations have already made their profit before the gasoline reaches the pump, they can afford to subsidize retail gasoline and carwash operations. There is no way they can make a profit by offering free carwashes.

And I can tell you that no independent carwash, whether they sell gas or not, can survive against this kind of competition. If this situation is allowed to continue, the small independent carwash and the small independent gas station will be driven out of business. Then the energy corporations will be able to raise prices for both carwashing and gasoline without fear of competition. No small businessman would dare to enter the industry knowing that the refiner-dealers have the resources to cut prices again and drive away all potential independent competition.

This predatory price-cutting is not unique to the retail gasoline or carwash industry. It is harmful not just to the small businesses that have served their communities for years, but also to the operation of the free market, the principles of open and fair competition on which our economy is based, and the interests of the con-

sumer. But we need legislative relief soon. Once our small businesses are forced to close down, it will be too late.

I would be happy to answer any questions you might have.

I also would like to enter into the record a couple of letters from independent carwash operators, along with pictures of oil company-owned and operated service stations, where they are selling the gas for less than what the carwash operator is paying for it.

Senator MATHIAS. Unfortunately, the printed records do not contain photographic illustrations, but we are glad to accept the letters for the record, and we will be glad to accept the pictures for the use of the committee.

Mr. MILEN. Fine; thank you.

[The following was received for the record:]



CAR WASH ENTERPRISES, Inc.

4503 - 8th AVENUE NORTHWEST

SEATTLE, WASHINGTON 98107 • (206) 789 3700 / 1 800 552 0744

March 7, 1984

The Honorable Strom Thrumond
United State Senate
Washington, D.C. 20510

Re: Senate Bill S-40

Dear Senator Thrumond:

I strongly urge you to support Senate Bill S-40 and allow companies such as mine to fairly compete against major oil companies.

As an independent businessman, it is an absolutely insurmountable task for companies such as mine to compete with a retailing facility which is owned and operated by a major oil company.

To give you some background to my business, my company, which is owned by the undersigned, owns and operates 12 car wash/gasoline installations in the Seattle, Washington area. One of our facilities has both Shell and Texaco company-operated facilities with a "free car wash" located approximately one mile away from our location.

In another example, Texaco has built a facility directly across the street from ours, also offering a "free car wash" with any eight gallons of gas purchased. When Texaco opened this unit, they charged 99.9 cents for a gallon of regular, while at the same time my buying price for that same gallon of gas from Shell Oil was 1.021/per gallon! While I consider myself an aggressive and honest businessman, how can I possibly compete under such circumstances?

Texaco will be building another gasoline and car wash facility six blocks from another one of my locations in Auburn, Washington. They also will be building still another car wash near a facility I own in Seattle.

A further example is Shell's building a "free car wash" 14 blocks from yet another one of my locations.

"THE PROFESSIONAL CAR WASH PEOPLE"

Where the major oil companies such as Texaco and Shell have opened their "free car wash" operations, my business has been negatively affected anywhere from 20% to 40%. Senator, I as much as any other American believe in free enterprise and competition. However, in my strong view the major oil companies unfairly compete because they control the natural resource from the wellhead to the customer's gas tank.

In conclusion, I strongly ask that you vote for Senate Bill S-40 to stop the annihilation of the independent gasoline dealer and allied businesses. If you do not support Senate Bill S-40, I would appreciate the courtesy of your replying to me as to advice as to how I can compete and remain in business under such unfair circumstances.

Sincerely yours,

CAR WASH ENTERPRISES, INC.

Victor D. Odermat, President



car wash

March 9, 1984

The Senate Judiciary Committee:

I am writing to you to urge you to support Senate Bill S.40.

As briefly as possible I will give you facts which I think will help persuade you to support this bill.

Our company has been in the full service car wash business for 17 years. We have sold Texaco gasoline for 16 of those years. Currently we own and operate one car wash in Ft. Worth, Texas and two in Oklahoma City, Oklahoma.

Our highest volume year in Ft. Worth was 1972. We washed 169,211 cars and sold 2,335,515 gallons of gasoline as verified by the enclosed letter from Texaco. In 1973 Shell Oil Co. opened a company owned exterior car wash 200 feet west of our business and their policy was to wash cars free with a fill up of 10 gallons or more. Exxon Oil Co. opened an exterior car wash one block west of us in 1973 and washed cars for 99¢ with a fill up of 10 gallons or more. Our volume decreased rapidly in 1974 and since then we have been averaging about 900,000 gallons a year.

In 1983 in Ft. Worth we purchased 826,607 gallons of gasoline and washed 113,214 cars. To verify pricing in this area, I am enclosing pictures of Exxon, Shell and Texaco's advertised prices.

The oil companies have just recently moved into the Oklahoma City market with company owned car washes with Texaco being the most aggressive. Texaco has opened 14 units in about 18 months since the last part of 1982. Texaco spends \$700,000 to \$800,000 on each new unit.

Current tank wagon pricing to retailers in Texas with all taxes included for regular gas is: Exxon - \$1.014, Mobil - \$1.029, Shell - \$1.029, Gulf - \$1.029 and Texaco - \$1.06.

Head Office, Texas: 5829 Curzon • Ft. Worth, TX • 76107 • 732-8651
Locations in Texas & Oklahoma

Exxon, Mobil and Texaco also charge dealers a 3% fee for all company credit card purchases. The three companies do have rebate programs in Texas because of legislation passed in 1983, but their rebates only cover a portion of the 3% credit card cost.

I will give you figures on our Oklahoma City volumes that will illustrate what Texaco's policy of selling gasoline below our cost has done to us.

At our May Avenue Oklahoma City unit in 1982 we sold 987,599 gallons and washed 132,544 cars. In 1983 we dropped to 718,301 gallons and washed 118,960 cars. At our Penn Avenue Oklahoma City location in 1982 we sold 776,648 gallons and washed 93,000 cars. In 1983 volume dropped to 584,944 gallons and washed 77,416 cars.

Texaco's tank wagon price to dealers 3/7/84 was \$1.0368 for regular, \$1.0768 for lead free and \$1.1268 for super lead free. You will note on the pictures from Oklahoma City that at car washes regular is .999, lead free is \$1.079 and their car wash is free with any fill up.

I appreciate your time and hope that the above figures will illustrate that pricing to dealers at one figure and then undercutting that price in the oil company's own operation is unfair competition.

Sincerely yours,

H. C. Blakewell
H. C. Blakewell

Senator MATHIAS. Mr. Alford.

STATEMENT OF LLOYD B. ALFORD

Mr. ALFORD. Thank you, Mr. Chairman.

My name is Ben Alford, and I am from Baton Rouge, LA. My family and I have been in the carwash business since 1952.

I must say that at this time, my business is undergoing the most troubled period of its existence. With respect to my self-service carwash, I believe that the difficulty I am now facing is a direct result of the entry by the major oil companies into the self-service retail gasoline and carwash business.

I estimate that in the Metropolitan Baton Rouge area, there are at least 35 self-service gasoline and carwash facilities that are operated by the major oil companies, all of which offer a free carwash with a fill-up. At some stations, they are giving away a free carwash with a pack of cigarettes, a soda, or whatever. At others, a free carwash is given away just by driving onto the lot. In several instances, the majors operated facilities is right next to or just around the corner from a small, independent, self-service carwash operator who does not have gasoline pump facilities.

I have brought along some photographs which will illustrate this situation, which I will be glad to give to you, Senator.

It does not take much to imagine what will happen to the business of a carwash operator in such a case. Would you pay to have your car washed if you could go next door and fill your tank up—which you probably need to, anyway—and in the process, get a free carwash?

I know of at least two operators who have gone out of business, and everyone else has been hurt.

I have some gross figures I would like to give to you that will show you an example of this. In 1980, my self-service carwash grossed \$24,801.83. In 1981, we grossed \$35,373.58; in 1982, \$24,969.66, and in 1983, \$21,074.67.

As you can see, since the majors have reemerged in the carwash industry between 1981 and 1983, there has been a 40—percent decrease in my gross income.

I can only venture to say, sir, that I am very worried, and share what I believe to be the concern of other small businessmen such as myself, that if the majors are permitted to continue to be a presence in the self-service gasoline and carwash industry, the independent owners of carwash facilities would be forced out of business.

Thank you.

Senator MATHIAS. Thank you very much.

We would be glad to have the photographs and other materials you are offering.

[Prepared statement follows:]

TESTIMONY OF LLOYD B. ALFORD
ON BEHALF OF
THE INTERNATIONAL CARWASH ASSOCIATION/
NATIONAL CARWASH COUNCIL

Thank you, Mr. Chairman. It is an honor to testify in support of S. 40, the Small Business Motor Fuel Marketer Preservation Act.

My name is Ben Alford. I am an owner of three car washes in Baton Rouge, Louisiana, and a member of the International Carwash Association. My family and I have been in the car wash business since 1952. I must say that at this time my business is undergoing the most troubled period of its existence. With respect to my self-service car wash facility, I believe that the difficulty I am now facing is a direct result of the entry by major oil companies into the self-service retail gasoline and car wash business.

I recall that in the early 1970's, the majors started to move into the car wash industry in Baton Rouge. At that time they uniformly began giving away a free wash with a fill-up, at self-service prices. However, during the oil embargo there seemed to be a let-up in these activities by the majors; they seemed to stop construction of new car wash facilities at their retail gasoline stations.

The involvement of the majors started again in the 1980's, and we have been hit by a tidal wave of major-owned and operated self-service gasoline and car wash facilities. Once again, a free wash is being offered with a fill-up at self-service prices, and we simply cannot compete.

I estimate that in metropolitan Baton Rouge there are at least 35 self-service gasoline and car wash facilities that are operated by major oil companies, all of which offer a free wash with a fill-up. At some stations the car wash is given away with any purchase: a soda, a pack of cigarettes, whatever. At

others, a free wash is given away--just for driving onto the major's property. In several instances, the major-operated facility is right next to or just around the corner from the small, independent self-service car wash operation that does not have gasoline pump facilities. (I have brought some photographs which illustrate this situation.) It doesn't take much to imagine what ^{will} happen to the business of the car wash operator in such a case--would you pay to have your car washed if you could go next door and fill up your tank, which you probably need to do anyway, and in the process have your car washed for free? I know of at least two operations that have gone out of business, and everyone else has been hurt.

I believe the gross figures from the operation of my self-service facility over the past four years provide a dramatic example of what is happening to the independent car wash industry.

Gross Income

<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>
\$24,801.83	\$35,373.58	\$24,969.66	\$21,074.67

As you can see, since the majors have reemerged in the car wash industry, between 1981 and 1983, there has been a 40% decrease in my gross income.

I can only venture to say that I am very worried, and share, what I believe to be, the concern of other small businessmen such as myself, that if the majors are permitted to continue to be a presence in the self-service gasoline and car wash industry, the independent owners of car wash facilities will be forced out of business.

I would be happy to answer any questions you or your colleagues might have.

PRICE OF GASOLINE

Senator MATHIAS. Thank you very much, gentlemen.

What I would like to do, and what I am sure other members of the committee who are detained on other business this morning would like to do is to review your written statements and then, if there are questions, to submit those questions to you in writing, and the questions and the answers will become part of the record.

I would have just one question to ask you directly this morning, and it is a question that does not really relate to S. 40, but it is a question in which I think the people of this country would be intensely interested.

We have all noticed, as we drive up to the gas pumps week by week, that prices are inching up again. What is your explanation for that?

Mr. ALFORD. Senator, in our area, the prices have gone down.

Senator MATHIAS. Well, you are fortunate people, then. Of course, you have your own.

Mr. MILEN. The only other explanation, Senator, is contact the major oil companies and find out why they continue raising, especially on the holidays, when motor traffic is going to be increased, and that is when they want to make their extra profit.

Mr. HOUSTON. Mr. Chairman, in Georgia in particular—I have been there 28 years, representing these people, so I keep a fairly close tab—there is an indication that every time the price increases on the pump, it is a direct result of an increase in the wholesale price or a cost factor imposed by a refiner. So I submit that you need to ask the refiner that question as to why he did raise that price.

Mr. RASHEED. Mr. Chairman, I believe we have had a glut situation. We also have oil companies waiting in the wings for any opportunity to try to raise that price. I think that any time you hear stories or read stories where the Strait of Hormuz may be closed, or something like that happens, you immediately see a reaction on the spot market, in New York Harbor or wherever. It takes very little to trigger an increase in the price of gasoline. They are certainly not going to wait until a shortage develops. It could happen even on a rumor. And I think the oil companies are working that rumor for all they are worth at this time.

Senator MATHIAS. I thank you very much, and if you have further thoughts on that subject or on other subjects, we will be glad to include them in the record.

Yes?

Mr. MOLNER. I think it is very important to remember that we are still the captive customer of the oil companies, and when they call and they say the price has gone up 2 cents per gallon, it is not the dealer putting the price up; it is the oil company. You have addressed it to the wrong people.

Senator MATHIAS. Well, we will address that to the next panel, who are waiting in the wings at this moment.

The next panel will include Mr. Nicholson, vice president of marketing for Marathon; Mr. Edward G. Reilly, vice president for retail marketing for ARCO; Professor John Umbeck, department of economics, at Purdue University; Mr. Timothy Columbus, counsel

for the Society of Independent Gasoline Marketers of America; and Mr. Phil Chisholm, executive vice president of the National Oil Jobbers Council.

Gentlemen, I will have to enforce the 5-minute rule just as strictly on you as I did on the previous panel.

Please proceed.

STATEMENT OF A PANEL, INCLUDING G. NORMAN NICHOLSON, VICE PRESIDENT, MARKETING, MARATHON OIL CO., WASHINGTON, DC; EDWARD G. REILLY, VICE PRESIDENT FOR RETAIL MARKETING, ARCO PETROLEUM PRODUCTS CO., WASHINGTON, DC; PROFESSOR JOHN R. UMBECK, DEPARTMENT OF ECONOMICS, PURDUE UNIVERSITY, LAFAYETTE, IN; R. TIMOTHY COLUMBUS, COUNSEL, SOCIETY OF INDEPENDENT GASOLINE MARKETERS OF AMERICA, WASHINGTON, DC, AND PHILLIP R. CHISHOLM, EXECUTIVE VICE PRESIDENT, NATIONAL OIL JOBBERS COUNCIL, WASHINGTON, DC

Mr. NICHOLSON. Mr. Chairman, I will begin. I am G.N. Nicholson, vice president of marketing of Marathon Petroleum.

In 1983, Marathon sold about 3.7 billion gallons of gasoline, and more than 68 percent of our sales were made to independent businessmen. That group includes approximately 2,200 Marathon-branded outlets in Indiana, Illinois, Kentucky, Ohio, Michigan and Wisconsin, which are operated by independent operators primarily as full-service stations. It also includes independent marketers who resell gasoline under their own private brands. The remaining 32 percent of our gasoline in 1983 was sold through a wholly-owned subsidiary engaged in direct retailing under secondary brand names.

It is undeniable that the gasoline marketplace has been changed during the last decade. Gasoline demand reached its peak in 1978. The total service station population has been dropping. The nature and composition of the outlets retailing gasoline today are vastly different from what they were 10 years ago. For example, 10 years ago, only about 20 percent of total gasoline sales was pumped through self-service units. Today, self-service accounts for over 70 percent of total sales. Ten years ago, the gasoline retailed by convenience stores represented a negligible share of the market. Today, this share of market claimed by convenience stores exceeds 7 percent and is still growing.

Today, the market share of branded and unbranded jobbers exceeds 46 percent versus 33 percent 10 years ago. Dealer's market share has fallen correspondingly. Market forces beyond the control of domestic refiners prompted consumers to use less gasoline and to shop for outlets offering lower prices when they did buy. The emergence of self-service as the dominant method of retailing gasoline is nothing more nor less than a competitive market's response to a consumer-driven change in buying priorities. As the gasoline market has changed, Marathon has not neglected its dealer network. We have more Marathon brand stations today than at the end of 1981. We have negotiated 380 new dealer leases, excluding renewals, since the beginning of 1979. We are currently seeking dealers for 32 locations. In the last 2 years, we have taken on as

new Marathon-branded dealers 98 former dealers of other companies who have withdrawn from the Great Lakes area.

All of our approximately 2,200 Marathon brand stations are operated by independent businessmen, jobbers, distributors, and dealers. There are no company-operated Marathon brand stations. These are almost entirely full-service stations. They receive the value of Marathon brand name, advertising, credit cards, dealer training, and all of the other services attendant to a Marathon-branded station. Even the gasolines they sell are different and better from those sold to our subsidiary and unbranded customers.

It is important that the subcommittee should clearly understand that this legislation does not prohibit oil refiners from operating retail gasoline stations. All but 22 of the more than 150 refiners in the United States are excluded under the small refiner exemption. Of the remaining 22 refiners, 7 would also be exempted from the divorcement, not on the basis of their size of identification with company operations in their gasoline retail marketing, but rather, on the completely irrelevant basis of the percentage of the refinery crude oil input purchased from third parties in 1978.

S. 40 would compel divorcement of just about half of the 15,955 company-operated outlets which exist today. Because of the refiners affected and the concentration of more than 7,500 of their company-operated outlets in the Midwestern States of Ohio, Michigan, Wisconsin, Indiana, Kentucky, and Illinois, the impact of S. 40's divorcement provisions would be essentially regional rather than national.

It is especially important for this subcommittee to know that since 1979, the legislatures of all of these most heavily impacted States have considered and rejected divorcement proposals similar to S. 40.

If the divorcement provisions of S. 40 were enacted, they promise no cure for the ailments of dealers. It must be evident that the elimination of some suppliers and some low-price marketers cannot promote or enhance competition. It is the consumer and the public interest which ultimately pay the cost of reduced competition. Such costs would come in the form of diminished purchasing options and higher prices.

For all these reasons, I urge you to reject S. 40.

Thank you.

Senator MATHIAS. Thank you very much.

[The following was received for the record:]

Statement of
G. NORMAN NICHOLSON
Vice President
Marketing, United States
Marathon Petroleum Company
Regarding
SMALL BUSINESS MOTOR FUEL MARKETER PRESERVATION ACT
(S. 40)
Before The
Subcommittee on Patents, Copyrights and Trademarks
Of The
Senate Judiciary Committee
March 14, 1984

I am G. N. Nicholson, Vice President, Marketing, Marathon Petroleum Company. I appreciate this opportunity to appear before the Subcommittee and express Marathon's views in opposition to S. 40. I ask that my entire statement be included as part of the record of this proceeding. I will summarize our views in the interest of time.

Marathon Petroleum Company engages in the refining, marketing and transportation of petroleum and petroleum products. It is a wholly-owned subsidiary of Marathon Oil Company. Marathon Oil's family of companies collectively make up a medium-sized integrated oil company which engages in virtually all functions of the oil business, including exploration and production, in the United States and abroad. Marathon Oil Company is owned by United States Steel Corporation.

Marathon Petroleum Company markets primarily in six Great Lakes states and in the southeastern region of the country. Over the years a very significant portion of Marathon's gasoline has been sold to independent marketers who resell the product under their own private brand names and to independent dealers, jobbers and distributors who resell the product under the Marathon trademark.

In 1983 we sold about 3.7 billion gallons of gasoline, and more than 68 percent of our sales were made to those independent businessmen. That group includes approximately 2,200 Marathon branded outlets in Indiana, Illinois, Kentucky, Ohio, Michigan and Wisconsin which are operated by independent marketers primarily as full-service stations.

The remaining 32 percent of our gasoline in 1983 was sold through a wholly-owned subsidiary engaged in direct retailing under secondary brand names such as "Bonded," "Castown," "Speedway" and "Cheker." At the end of 1983 the subsidiary operated approximately 1,200 of the secondary brand outlets which are primarily self-service "gas and go" units. It is this group of secondary brand outlets that would be directly affected by the divorcement provisions of S. 40.

It is undeniable that the gasoline marketplace has been characterized by unprecedented turbulence during the last decade. The total service station population has dropped dramatically. The nature and composition of the outlets retailing gasoline today are vastly different from what they were ten years ago. While there may be some dispute about exact numbers, the trends are clearly evident. We know, for example, that ten years ago only about 20 percent of total gasoline sales was pumped through self-service units. Today self-service accounts for over 70 percent of total sales. Ten years ago the gasoline retailed by convenience stores represented a negligible share of the market. Today the share of market claimed by convenience stores exceeds 7 percent and it is still growing.

The most definitive data has been collected by the Department of Energy in connection with its study and report to Congress as mandated by Title III of the Petroleum Marketing Practices Act. The DOE determined the relative shares of total gasoline sales made by the 28 largest refiners to various classes of trade on a year-by-year basis from 1972 through 1979.¹ These refiners' direct sales to commercial end users dropped from 9.6 percent of their total gasoline sales in 1972 to 5.7 percent in 1979. Sales to dealers directly supplied by those refiners dropped from 50.7 percent in 1972 to 36.9 percent in 1979, a loss of 13.8 percentage points. Gasoline sales by these 28 largest refiners through company-operated retail outlets increased from 6.6 percent of the total in 1972 to 11 percent in 1979. Sales to branded jobbers and unbranded independents, which represented 33 percent of the total in 1972, increased a whopping 13.4 percentage points to 46.4 percent of the total in 1979.

The Lundberg Letter of August 5, 1983, contains information about the population of gasoline retail outlets which allows us to update the trends through 1982. Lundberg's data show a reduction in the total number of retail outlets from 242,470 units at year-end 1980 to 210,875 units at year-end 1982. This represents about a 13 percent decrease for the two-year period. The number of outlets supplied directly by refiners and operated by lessee and contract dealers declined from 110,410 units in 1980 to 84,450 units at year-end 1982.

¹ Final Report, "The State of Competition in Gasoline Marketing," Department of Energy, January 1981, p. 111.

Likewise, the number of units company-operated by refiners dropped from 16,910 units in 1980 to 15,955 units by year-end 1982. The number of jobber and private brand independent marketer outlets also declined from 115,150 units in 1980 to 110,470 units at year-end 1982. Thus, of the 210,875 total gasoline outlets operating at year-end 1982, 52.4 percent were supplied and operated by jobbers and private-brand independent marketers; 40 percent were operated by lessee and contract dealers of refiners; and only 7.5 percent were company-operated by refiners.

These data certainly confirm that an upheaval has occurred in gasoline retailing over the last decade. Everyone agrees on this. Disagreement begins with explanations of the causes of the upheaval and with possible cures.

Those of us who oppose S. 40 are convinced that the turmoil which has been experienced in the gasoline marketplace during the last decade can be fully explained in terms of natural adjustments to drastically changed market conditions and competitive forces. It is a classic, textbook example of the way a competitive market, thrown into disequilibrium by new forces beyond the control of the competing sellers, adjusts itself toward a new supply/demand equilibrium among buyers and sellers. There are survivors and losers in this normal adjustment process, but there are no villains -- as S. 40 presupposes -- because the factors producing responsive changes lie beyond the reach and control of any of the gasoline competitors themselves.

Those who support S. 40 argue that sinister strategies and unfair marketing practices on the part of refiners are responsible for the disappearance of thousands of dealers from the marketplace and for the competitive problems facing those who remain. They imply that all refiners are employing the same monolithic strategy, despite DOE findings that refiners were employing several different marketing strategies. It may be simple, convenient and appealing to some to explain the turbulence of the gasoline marketplace in terms of wrongdoing Goliaths and victimized Davids, for such a simple explanation suggests a simple cure: banish the Goliaths and you perforce preserve the Davids. But this simple explanation of cause and effect -- which provides the only rationale for the punishment that the divorcement provisions of S. 40 would inflict -- is both wrong and reckless. It is wrong because it is contradicted by the known data. It is reckless because it so blithely ignores all the other factors and changing conditions which have actually caused the competitive problems of dealers.

Understanding what has happened to gasoline dealers over the last decade begins with understanding that, dating from the Arab Embargo in 1973, the entire oil industry has been shaken from top to bottom. The center of the storm does not lie in the gasoline market, as supporters of S. 40 would have you believe; and dealers have by no means been the only players adversely affected. Over the course of the last several years changed economics have forced thousands of independent producers out of business. Hundreds of suppliers of oil field goods and services have declared bankruptcy. On January 1, 1981, there were 324 refineries operating in the United States.

By January 1, 1983, this number had been reduced to 258. The 66 refineries which were shut down represented a two-year attrition rate exceeding 20 percent, and 10 of these had daily distillation capacities of 50,000 barrels per day or more. During 1983, another 11 refineries and parts of others shut down. Since January 1, 1981, the primary crude oil distillation capacity of U.S. refineries has fallen from 18.6 million barrels per day to 15.9, over a 14.5 percent loss in three years. With refining operating rates on average fluctuating between roughly 64 and 75 percent of capacity in recent months, the shakeout in refining probably hasn't yet completed its course.

It should be obvious from these facts that the upheaval of the last decade has been much wider and deeper than gasoline retailing alone, and that dealers have not been uniquely its victims. It has taken its toll in all segments of the oil industry, especially among refiners.

Now I want to turn to a closer inspection of the available data concerning station population and market shares. If it were true, as supporters of S. 40 claim, that a cause-and-effect relationship exists between refiners' alleged unsavory practices and the marketplace losses suffered by dealers, then we should expect the data to show some correlation between the gains in refiners' company-operated outlets and dealers' losses. We should also expect the data to show refiners gaining at the expense of other non-refiner retailers because the unfair marketing practices which have been charged, if true, would be indiscriminate in their adverse impact on all other competitors in a given market.

But the data reject the claim. DOE data for the 28 largest refiners show that, as a percentage of their total gasoline sold, sales through company-operated units climbed from 6.6 percent in 1972 to 11 percent in 1979 -- a gain of only 4.4 percentage points. In this same timeframe, sales through dealer-operated stations dropped 13.8 percentage points -- from 50.7 percent to 36.9 percent. And during this same time span, the sales through branded jobbers and unbranded independents jumped 13.4 percentage points -- from 33 percent to 46.4 percent of the total.

It is self-evident from these figures that the market gains enjoyed by jobbers and independent marketers almost exactly match the losses sustained by dealer-operated stations. On the other hand, the gains experienced by refiner-operated outlets represent less than one-third the losses borne by dealer-operated units. In the face of such facts, it is just inconceivable that the plight of dealers can be traced to alleged "predatory practices" of refiners. By definition, a predator injures all of his competitors by his unfair practices. If refiners generally were guilty of the predatory practices claimed by the supporters of S. 40, then it would have been impossible for jobbers and independent marketers to pick up three gallons of additional market share for every one gallon gained by the alleged predators. The jobbers and independent marketers were obviously doing something right. Their market share gains from 1972 to 1980 prove that they were by far the most successful among all gasoline retailers in adapting to the drastically changed conditions of the marketplace.

Yet the supporters of S. 40 do not charge this most aggressive and successful group of retailing competitors of any wrongdoing, nor do such supporters even openly recognize and admit the achievements of these highly successful competitors. Instead, they conveniently ignore jobbers and independent marketers as competitive factors in order to concentrate blame on refiners.

What has happened since 1980 does not alter this basic picture. The Lundberg data on station population confirm that from the end of 1980 to year-end 1982 the number of refiner-operated outlets actually decreased from 16,910 units to 15,955 units. At that number they represented only 7.5 percent of the total 210,875 gasoline retail outlets in operation at year-end 1982. These data -- coupled with the fact that market gains by jobbers and independent marketers have placed them in the position of operating more than half of all gasoline retail outlets since 1980 -- should put to rest the notion that refiner-operated units have made sizable gains in, much less taken over, gasoline retailing.

The conclusions just stated are entirely consistent with those contained in the Final Report of the DOE published in January 1981 on "The State of Competition in Gasoline Marketing." After thorough investigation and study, the DOE stated unequivocally that charges of subsidization, "predatory pricing" and "predatory costing" by refiners in their operation of retail gasoline outlets were unsubstantiated by any credible evidence and unfounded.

There is another basic flaw in the argument that refiners are deliberately driving dealers out of business in order to company-operate the outlets thus abandoned by dealers.

Such a strategy simply could not be implemented on a wide-scale basis because it is unlawful under the Petroleum Marketing Practices Act of 1978. That Act explicitly prohibits a refiner from canceling or failing to renew a franchise with a dealer in order to convert the outlet to a company-operated unit.

There are, of course, logical and valid explanations for the competitive problems which have confronted dealers and which have resulted in a declining population of dealer-operated retail stations.

The explanations are to be found in four basic competitive factors:

1. A decline in total gasoline consumption.
2. Significantly reduced demand at service stations for automotive goods and repairs.
3. A dramatic shift in the buying preferences of motorists in favor of self-service outlets offering lower prices.
4. Major changes in the regulatory environment.

Total gasoline consumption -- and with it service station population -- rose steadily until 1973. Consumption declined in 1974 and then began a gradual climb to 1978 when annual consumption peaked at a little over 115 billion gallons. Consumption has declined each year since 1978 in a trend that is expected to continue until 1990. Consumption in 1982 of just over 100 billion gallons roughly equalled the consumption of ten years earlier. The steadily diminishing gasoline consumption since 1978 would dictate the closure of a roughly corresponding percentage of retail outlets -- something in the order of 15 percent.

The average full-service station -- the kind most commonly operated by dealers -- depends on three basic sources of revenue for survival: gasoline sales, automotive repairs and sales of automotive parts and accessories. Other types of retail outlets -- convenience stores, self-serve units and car washes -- do not have this dependency on repairs and TBA sales for good health.

Changing market conditions have severely eroded the business done at service stations over the past several years in automotive repairs and TBA sales. A few examples will serve to highlight the nature and degree of erosion in these non-gasoline lines of business. Service stations enjoyed a 45 percent share of all motor oil sales in 1971. This fell to 24 percent in 1981. Mass merchandisers captured the business. Service stations made 15 percent of all battery sales in 1970, but only 6 percent in 1981 -- business lost to battery specialists and mass merchandisers. In the replacement tire market, the share of total sales claimed by service stations dropped from 19 percent in 1975 to just 12 percent in 1980 -- business lost to tire dealers. Service stations performed over 20 percent of car tune-ups in 1974, but only 14 percent in 1981. The phenomenal growth in specialty shops and auto centers -- which offer cost and time-saving advantages and often convenient shopping center locations -- has come largely at the expense of service station dealers. Midas Muffler has grown from 877 shops in 1977 to 1,200 in 1981; AAMCO Transmissions had 523 franchises in 1975 versus 930 in 1982; Firestone offers general repair services in its 1,400 auto centers and 434 J. C. Penney locations; Sears and Montgomery Ward operate 850 and 211 auto repair centers, respectively.

Even in a stable gasoline market, the inroads made by these specialty parts and repair businesses would have been enough to cause thousands of dealers to fail.

The third market factor which explains the difficulties of dealers is the massive shift in the buying preferences of motorists to self-serve outlets offering lower prices. Self-serve gallonage has grown from 20 percent of the market ten years ago to roughly 70 percent today. It requires no deep probing to discover why this shift has occurred. The four-fold increase in gasoline prices which followed in the wake of the 1973 Arab Embargo has made price a dominant factor in most motorists' buying patterns -- and generally the lowest prices are to be found at self-serve units.

It is thus apparent that market forces beyond the control of domestic refiners prompted consumers to use less gasoline and to shop for outlets offering lower prices when they did buy. The emergence of self-serve as the dominant method of retailing gasoline is nothing more nor less than a competitive market's response to a consumer-driven change in buying priorities. And no amount of government tampering can force price-conscious motorists into the driveways of those full-service stations where prices are higher.

Marathon's experience has mirrored the market transition. Direct retailing did not become a part of Marathon's marketing strategy until the early 1970s. At that time it became evident to us that consumer buying habits were changing. Many of our dealers lost gallonage, backroom repair trade and TBA sales. An unprecedented number of our dealers failed, forcing us to close units in which we had large investments.

At the same time, our wholesale sales to unbranded marketers who were mainly discount retailers, together with other evidence, left no doubt that they were picking up gasoline customers our dealers were losing. The message which consumers were giving to Marathon and other similarly situated medium-sized refiners was unmistakable -- adapt to the changing buying preferences or face a declining and potentially unprofitable marketing business. Marathon did respond by creating a viable direct-retailing network. By catering to the preferences of those customers who patronized us, we have preserved for Marathon a little over a billion gallon share of the annual gasoline market which otherwise certainly would have been lost to other competitors.

Having said this, I would be remiss if I left you with the impression that Marathon has neglected its dealer network. Contrary to general industry trends, we have more Marathon brand stations in operation today than at the end of 1981. We have negotiated 380 new dealer leases, excluding renewals, since the beginning of 1979. We are currently seeking dealers for 32 locations. In the last two years we have taken on as new Marathon branded dealers 98 former dealers of other companies who have withdrawn from the Great Lakes area. All of our approximately 2,200 Marathon brand stations are operated by independent businessmen -- jobbers, distributors and dealers. There are no company-operated Marathon brand stations. These are almost entirely full-service stations. They receive the value of the Marathon brand name, advertising, credit cards, dealer training and all of the other services attendant to a Marathon branded station. Even the gasolines they sell are different from those sold to our subsidiary and unbranded customers.

These gasolines are of higher quality, containing additives designed to clean and reduce deposit buildup in intake systems, prevent rust formation in vehicle fuel tanks and assure better fuel economy -- and they are advertised as such by Marathon. It is this type of branded station which we believe will appeal to an important market segment comprised of those consumers who are looking for added value in products and service and are willing to pay a little extra for it. You will recognize and appreciate that Marathon's marketing strategy is absolutely inconsistent with the accusation that we are trying to drive dealers out of business.

The fourth major factor affecting gasoline marketing during the last decade has been the government regulatory environment. The distorting effects of government regulations were capsulized by the DOE in its Final Report to Congress in January 1981 as required by Title III of the Petroleum Marketing Practices Act. It stated:

Most domestic crude oil and many petroleum products, including gasoline, have been subject to price controls since Phase I of the Nixon Administration's inflation control effort in 1971. The Emergency Petroleum Allocation Act of 1973 (EPAA) authorized the Department to directly regulate gasoline supplies and prices. Even though it appeared that the trend to larger volume outlets was underway before these various price and allocation regulations were adopted, the regulations did not have a neutral effect in the marketplace. For example, some of the most important regulatory effects include:

- ° The supplier/purchaser freeze and an allocation system that appears to have favored certain classes of trade at the expense of others. This system was complicated by the equal application rule, guidelines for distributing so-called surplus product, and constant reinterpretation of rules governing new outlet allocations.

- ° A freeze of prices between suppliers and purchasers with a cost passthrough system that maintained price differentials between classes of trade at their historical level.
- ° A freeze on dealer rentals until November 1975. This reduced the benefits of a dealer system to a refiner.

While each of these regulations had specific effects on individual dealers and other independent marketers, they also created a distortion common to all administrative regulations, the prevention of adjustments to underlying market forces. In a dynamic market, such as gasoline marketing, this can impose heavy costs on consumers. There is no doubt that the regulations benefited individual marketers, while they burdened other marketers. The exact calculus of benefits and costs cannot be precisely determined.²

The removal of price and allocation controls at the end of January 1981 released all the pent-up pressures on refiners and marketers to adjust rapidly to the new dynamics of the marketplace. Adjustments that would have occurred gradually but for government controls have been compressed into a short time span characterized by market withdrawals, realignment of relationships and the sudden elimination of many refiners, wholesalers and retailers -- all made more turbulent because of its speed and more painful because it coincided with a general economic recession.

I have now explained Marathon's view of the gasoline and related markets -- how and why they have changed, and our responsive strategy to cope with those changes.

² Final Report, "The State of Competition in Gasoline Marketing," U.S. Department of Energy, January 1981, p. 210.

I have also dealt with the charges of refiner misconduct in the market which have obviously fueled the legislative proposal before you, and have shown that those charges cannot possibly be true. For emphasis, it should be noted that these misconduct charges have all been investigated and analyzed thoroughly by the Department of Energy, the Federal Trade Commission and the Department of Justice who found the charges to be utterly without support or merit, and who recommended against structural remedies in the gasoline market as S. 40 would impose.

The supporters of S. 40 may point to the potential advantages dealers and other non-refiner marketers would gain if certain refiners are prohibited from retailing gasoline. But there's another side to this coin that your members probably do not fully appreciate. This is the damage S. 40 would inflict on the affected refiners and the consuming public. In Marathon's case, the approximately 1,200 units operated by our subsidiary are valued at substantially in excess of \$190 million. They employ over 6,400 people and serve customers who buy over 1.3 billion gallons of gasoline annually. It is impractical to convert these units to dealer operation. Divorcement, therefore, would almost certainly equate to divestiture which would jeopardize the jobs of the 6,400 employees and devalue our investment to a fraction of its real worth. With over one billion gallons of gasoline potentially searching for a home, both our refining and marketing operations would be severely threatened. The forced sale of these units to other refiners who are excluded from divorcement, or jobbers, or chain marketers would virtually assure that they would continue to be operated through employees as high-volume, low-margin outlets.

This would be a financial windfall for the buyers, but it would do nothing to ease the plight of dealers. When you realize that Marathon represents only a small percentage of the outlets that would be affected by the divorcement provisions of S. 40, you begin to understand the magnitude and dimensions of the damage that S. 40 would inflict on the gasoline marketplace. They are staggering.

The divorcement provisions extend even further than this for affected refiners. They would also reach such a refiner's investment interest in affiliated, non-controlled marketing companies. If such a refiner owns the "single largest share" of the stock of another corporation which operates retail gasoline stations, such corporation will be deemed to be a "related person" and prohibited from continuing direct operation of its retail stations. It does not matter whether the refiner's interest is active or simply a passive investment. It does not even matter whether the refiner does or can legally, either through a majority stock position, contract or otherwise, control the operations of the affiliated corporation. All that matters is that the refiner owns the "single largest share" of stock. One wonders how a 50-50 joint venture would be treated under this test.

The Subcommittee should clearly understand that this legislation does not prohibit all refiners from operating retail gasoline stations. All but 22 of the more than 150 refiners in the United States are excluded under the "small refiner" exemption.

Of the remaining 22 refiners, several would also be exempted from divorcement not on the basis of their size or identification with company operations in their gasoline retail marketing, but rather on the completely irrelevant basis of the percentage of their refinery crude oil input purchased from third parties in 1978. This is a ridiculous classification utterly devoid of rhyme or reason.

Just how illogical, arbitrary and capricious S. 40's selection of divorcement candidates is can be easily demonstrated. First, the eight largest refiners -- all divorcement candidates -- are as a group least identified with gasoline retailing through company-operated units. They sold only 4 percent of their sales through such units compared to the national average of 11 percent. Several of these eight operate no company stores at all other than training facilities.

Second, retailing through refiner-operated units is a marketing method practiced far more by small and medium-sized refiners than "Big Oil." It is a strategy employed only by a few of the 40 largest refiners, and is far from a universal practice. Between 1972 and 1978, DOE data show the total gallonage sold by refiner-operated units increased 6.9 billion gallons. Twenty of the 40 largest refiners accounted for 6.7 billion gallons (or 96.6 percent) of this increase. Of those 20 refiners described as "prime movers" by the DOE, less than half would be forced to divorce their retail units under S. 40.³

³ Final Report, "The State of Competition in Gasoline Marketing," Department of Energy, January 1981, Table 4-4.

The divorcee candidates would be: Marathon, Gulf, Sohio, Mobil, Conoco, Arco, Sun and Union. Among the prime movers who presumably would escape divorcee under S. 40 exemptions are: Clark, Southland (formerly Citgo), Vickers, Ashland, Hess, Tenneco, Tosco, Crown, United Refining, Tesoro, Total and Little America.

Third, because of this unreasonable hit-and-miss selection process, S. 40 would compel divorcee of just about half of the 15,955 company-operated outlets which exist today. Because of the refiners affected and the clustering of more than 7,500 of their company-operated outlets in the midwestern states of Ohio, Michigan, Wisconsin, Indiana, Kentucky and Illinois plus the states of Virginia and West Virginia, the impact of S. 40's divorcee provisions would be essentially regional rather than national in scope and would be concentrated primarily in these eight states. It is especially important for this Subcommittee to know that since 1979 the legislatures of all of these most heavily impacted states have considered and rejected divorcee proposals similar to S. 40. Enactment of S. 40 would thus be tantamount to overriding the legislative will of these states and what they regard to be in their best public interest.

Before closing, let me say a couple of things about the "open supply" provision of S. 40. This provision -- which would permit a dealer to shop suppliers for the lowest price gasoline and resell it in a branded station -- would create havoc in the branded marketing system and could cause many refiners to abandon it.

The Dealer Tankwagon Price is a package price which a dealer pays for gasoline delivered from the rack to the dealer's station enhanced by the added values of the refiner's trademark and credit card usage and a bundle of branding services which supports and benefits the dealer. In Marathon's case, as I pointed out earlier, our branded dealers, jobbers and distributors even receive different and better gasolines than we sell to our unbranded customers. Because the rack price represents the commodity price of unbranded gasoline only and available only at the rack, such a price will normally be lower than the DTW in the same area on a given day. Thus, a dealer could theoretically buy unbranded gasoline at the rack from us at a price lower than his suppliers' DTW, and this same would hold true for our dealers buying unbranded gasoline at the rack from other suppliers. But the comparison is like apples and oranges. They are not the same, but S. 40 would decree the differences to be irrelevant. If my dealer can buy oranges from another supplier cheaper than he can buy apples from me, then S. 40 would free him from his contract to buy my apples so he could buy and resell oranges at my apple stand. This is unfair, and I would be hard-pressed to justify continued investments in apple stands.

In conclusion, the decline in service station population and the competitive problems facing dealers have not been caused by refiner misconduct or their operation of retail outlets. The divorcement provisions of S. 40 would inflict punishment without a related crime. The causes of dealers' competitive problems extend beyond gasoline retailing per se.

Their full-service operations have suffered uniquely from the losses in trade of automotive repairs and TBA sales. Their losses in gasoline trade is traceable to changing consumer preferences, not to unsavory practices of their competitors.

If the divorcement provisions of S. 40 were enacted, they promise no cure for the ailments of dealers. While the legislation would be economically devastating to medium-sized refiners like Marathon who would be disproportionately affected, the outlets they could no longer operate would almost certainly find their way into the hands of exempt refiners, chain retailers, jobbers and private brand independent marketers. They would benefit from a windfall of cheap, forced sales; but in the end the dealers would not be better off. Indeed, it is not far-fetched to postulate that the chain of events set in motion by S. 40 divorcement could lead to greater concentration of retailers and an accelerated loss in market share of dealers.

It must be evident that the elimination of some suppliers and some low-price marketers cannot promote or enhance competition. Divorcement blatantly aims to protect a special class of competitors at the expense of other competitors and competition itself. This is not to say that competition would be destroyed by such action, but it certainly would be diminished. And it is the consumer and the public interest which ultimately pay the costs of reduced competition. Such costs would come in the form of diminished purchasing options and higher prices.

For all these reasons, I urge you to reject S. 40.

Thank you. I will be happy to answer any questions you have.

Senator MATHIAS. Mr. Umbeck.

STATEMENT OF JOHN R. UMBECK

Mr. UMBECK. Thank you, Senator.

My name is John Umbeck. I am a research economist at Purdue University.

I first became interested in divorcement back in Indiana 2½ years ago, when I heard the dealers claim that they were being driven out of business by exceptionally low prices being charged at company-operated stations. However, I became puzzled when they then went on to claim that divorcement, if passed, would increase competition and lower prices even further. It became even less clear what was happening when Mr. Arthur Price testified that in Maryland, where they had experienced divorcement for several years, they had in fact found that prices had gone down.

As an economist, this was a puzzling observation, and so we started our own investigation at Purdue of the Maryland experience. We first identified those stations in Maryland that had been affected by divorcement, a little over 200 of these stations. We tracked approximately 150 of these stations over a 5-year period, measuring their retail pump prices and a number of other services, including hours and so on, that these stations were operated. In addition, we surveyed the local markets around each of these 150 stations to get the price reactions of the lessee dealers as competitors in this marketplace.

The complete study has been submitted to you—actually, a summary of the complete study. I can make available to you upon request the 60-page document, but I would not recommend reading that unless you are having trouble going to sleep some night. It is excruciating detail of the methodology and the statistical procedures we went through.

Senator MATHIAS. That is why economics is a dismal science.

Mr. UMBECK. A well-deserved reputation.

The bottom line was this. We found at the divorced stations in Maryland that they were in fact charging prices below that of the average lessee dealer in the same marketplace—approximately 1½ cents below on self-serve, and approximately 3 cents lower on full-serve. This was before divorcement.

Immediately follow divorcement, we found that the average divorced station now operated by a lessee dealer increased their prices over 2 cents on self-serve, and almost 6 cents on full-serve.

In the nearby market, the other lessee dealers who were unaffected initially by divorcement were then able to raise their prices almost a full penny on self-serve and almost 3 cents on full-serve.

In addition to this, we found that at the divorced station now under lessee dealer operation, the average weekly hours declined by 7.9 per week.

Our conclusion is that divorcement in the State of Maryland did cause higher prices immediately following divorcement.

This, however, does not resolve the question of what is causing these lower prices. In other words, if it was predatory pricing, and divorcement had eliminated predation, then in fact, we would have observed prices going up, which is what we observed. If it was com-

petitive, a more efficient way to operate a station, and the law eliminated those stations, then we would also find higher prices. So the next question that we were left to resolve as researchers was what was causing this noticed price increase.

Now, predation is a very touchy subject. Economists have been trying to get a handle on this for over 20 years. It is difficult to find a test which will allow us to discriminate between these two competing theories—competition versus predation. However, the State of Delaware offered us a unique test of these two competing theories. In Delaware, they have had divorcement since 1974. However, it was not complete divorcement. They allowed, with a grandfather clause, existing company-operated stations to remain, but new company-operated stations would not be allowed to open.

What this means is if you understand the theory of predation, it says that the oil companies will deliberately charge a very low price, take losses in their company-operated stations, for a short period of time to drive the lessee dealers out of the market and then raise their prices to much higher levels to compensate them for this predatory price war.

The key is here that you have to have some future gain expected in order to make the price war a viable, profitable economic undertaking.

I will be done in just one minute——

Senator MATHIAS. Thirty seconds.

Mr. UMBECK. What we found in Delaware, where there was no hope of monopolizing the market because of divorcement—no new stations would be allowed to enter—we found still company—operated stations offer significantly lower prices than lessee dealers. We are therefore forced to conclude that there is no evidence of predation in these retail markets. What is most likely is this is merely a more efficient way of operating gas stations under some circumstances. The higher prices in Maryland, if extrapolated nationwide under your divorcement bill, will cost consumers approximately \$1 billion extra dollars per year for their gasoline purchases.

Thank you.

Senator MATHIAS. Thank you, Professor.

[The following was received for the record:]

TESTIMONY ON SENATE BILL 40
"SMALL BUSINESS MOTOR FUEL MARKETER PRESERVATION ACT"
TO BE PRESENTED MARCH 14, 1984

BY

PROFESSOR JOHN R. UMBECK

PURDUE UNIVERSITY

Members of the Committee on the Judiciary, my name is John Umbeck. I have been asked by the Atlantic Richfield Company to present to you the results of some of my research in retail gasoline marketing. I am not an expert on the petroleum industry. As my resume will show, I am an expert on the economic effects of regulations. This is the area of research in which I have spent most of my professional life.

The bill which is before us today is an attempt to deal with the problem of declining numbers of independent gasoline retailers. The fact that the number of lessee-dealers has been reduced dramatically over the last decade is agreed upon by both the proponents and the opponents of this bill. However, it is claimed that this decline is different from the declines which have been observed in other industries. For instance, when mass production of the automobile was begun, we observed the economic demise of the black smith as his services were no longer demanded by the public.

The proponents of divorcement legislation are claiming that big oil companies are driving them out of the market by subsidizing their salary-operated stations. Faced with this low predatory price competition, the lessee-dealer is forced to lower his gasoline prices and take a loss. Since the average dealer can not afford to incur these losses for very long, he is eventually forced to close his station. Only by divorcing "big oil" out of retail marketing can the small lessee-dealer survive.

Within this argument there are two issues which I would like to address as an economist. The first issue is the one of alleged predation on the part of "big oil". The second issue is the effects of divorcement legislation on the retail petroleum market. Over the last 2 years I have done extensive research in both of these areas.

THE EFFECTS OF DIVORCEMENT LEGISLATION

I first became interested in the retail petroleum market when I heard Mr. Arthur Price testify in Indiana on the Maryland divorcement experience. He claimed that unfair, predatory pricing precipitated divorcement legislation in Maryland. As a result of this legislation, he further claimed, average retail gasoline prices fell. Of course, this is logically impossible. If divorcement eliminated the lowest priced gasoline (which must have been the case if there was predation at the refiner-operated stations as Mr. Price stated), then the average price must have increased.

This logical contradiction stirred my curiosity. I began a careful study of the Maryland petroleum market in the fall of 1981. The methodology and the results of that and subsequent studies are presented in detail in the report that I have made available to you. Rather than bore you with all of the details, I will present only our basic findings. We found that divorcement in Maryland led to fewer stations, shorter hours at the divorced stations and significantly higher prices at both the divorced stations and their nearby, lessee-dealer competitors.

These results should come as no surprise to anyone. When a law eliminates the lowest priced sellers from a market we should expect the average price to increase in that market. This would be true if there was predation and it would be true if there was competition.

What did surprise me was the response of the proponents of divorcement. When my results were made public, they claimed that D.O.E. regulations had caused the Maryland price increases. They stated that the government price controls on gasoline had prohibited refiners from marking up their gasoline at their company operated-stations by as large a margin as was allowed lessee-dealers. This restriction was in place prior to Maryland divorcement but was eliminated just after the legislation was put in effect. This, they argued, could have created the illusion that divorcement was responsible for the higher prices.

While their statement on the legal restrictions is correct, what is surprising is that they are now saying the low prices at the refiner operated-stations were not the result of predatory pricing. They were the result of government regulation. If this is the case, there is no reason to have divorcement legislation since the restrictions they are citing are no longer in place.

PREDATION AND GOVERNMENT REGULATION

Our study of the Maryland market revealed that gasoline prices increased following divorcement legislation. However, it was still not clear if this was caused by the elimination of government price regulation, the elimination of predatory pricing, or the elimination of competition. Our next research project was an attempt to answer these questions.

Testing for the effects of the D.O.E. regulations was relatively simple. These regulations were only binding when the retail prices of gasoline were at their legal ceiling. A careful inspection before and after divorcement in Maryland revealed the fact that retail gas prices were at their ceilings only from spring to winter of 1979. At other times, the availability of gas was keeping prices well below their legal limits. In other words,

retailers could charge whatever the market would allow; the price control was not a factor.

To see if government price controls had any effect on the price increases which were observed after divorcement, we merely dropped from our sample those prices which were at the ceiling. Dropping those price observations did not significantly effect our initial findings. Divorcement legislation, not price controls, caused the increase in Maryland gasoline prices.

Next, we tested for predation. This was much more difficult. For the last 20 years economists have debated the existence of predatory pricing in a number of industries. While most are agreed that it probably does not exist to any significant degree, it has proven difficult to empirically verify. The problem is that predation and competition will both lead to similar types of behavior in the market. For instance, if I have a monopoly in a particular market and charge a relatively high price, I will be forced to lower that price if a new competitor enters my market. This decrease in price could be predation or it could be the result of new competition. Now, after lowering my price, if my competition is driven out of the market because he is not as efficient as I am, I will raise my price. Again, this is consistent with both predation and competition.

However, the Maryland retail gasoline market provided a unique opportunity to test for predation. The logic of the test is very simple. In order for predatory pricing to be profitable, the refiners must lower their retail prices enough to drive out their competition and then raise prices to levels which now exceed the competitive market. Only if they can charge extra high prices in the future will predation pay. In July of 1978, the Supreme Court ordered oil companies to divorce their company stations within one year. This decision marked the end of the legal appeal process.

The oil companies had no legal alternatives remaining. On this date, any expectation of monopolizing the retail gas market in Maryland were shattered. Predatory pricing could no longer be expected to be profitable. If the refiners were charging prices below their costs before the courts decision, there would now be nothing to gain from taking any more losses. If there was predatory pricing we would have observed retail prices at those refiner-operated stations to increase in July of 1973.

In fact, immediately following the Supreme Court decision, there were no changes in the prices at the refiner stations. They continued to charge prices well below the average lessee-dealer right up to the date on which they were divorced. We are forced to conclude that these low prices were profitable and not the result of predatory intent.

Our experience suggests that refiner-operated stations charged lower prices because they were profitable to run in this way. These low prices were not the result of government price controls nor were they the result of predation.

THE DELAWARE EXPERIENCE

Last year I discovered another market where predation was alleged; the state of Delaware. Delaware, like Maryland, passed a divorce bill in 1974. However, unlike Maryland, this bill allowed existing refiner-operated stations to remain in the market, only new ones were prohibited.

This economic environment in Delaware allowed for yet another test of predation. Here we had a market which allowed some refiner-operated retail gasoline stations, but prohibited any new ones. In this market it was impossible for predation to succeed because even if low prices drove out your competition, you could

not expand your refiner-operated stations to capture this monopoly. If we observed these refiner-operated stations charging prices which were significantly lower than the average lessee-dealer, it could not be predatory.

The data for this test was collected through the University of Delaware. Using graduate students, almost every retail gas station in the state was surveyed. We obtained information on pump prices for self and full-serve gasoline, for all grades. In addition we know the hours they were open, the number of pumps and hoses, their credit card policy, including discounts for cash, the number of service bays, whether or not there was a convenience store and even the location of the station with respect to business, residence and freeway. We have this information for over 500 stations.

With this data on computer, we could now measure the effects of each of these variables on pump prices. For instance we could now estimate the value of credit at a station, or the value of its location with respect to freeways or other competitors. We could tell the value of a particular brand name, or whether having a service bay will increase the pump price.

Of particular importance is whether or not refiner-operated stations had lower prices than the average lessee-dealer. The answer is yes. While the number of refiner-operated stations in Delaware was relative small and they could not expand their numbers, they still charged lower prices than the lessee-dealer. Furthermore, this could not be caused by government price controls because this data was collected after deregulation.

To date, all of our studies have refuted the claim of predation. But if predation is not the cause of lower prices at refiner-operated stations, and it is not government price

controls, what is the explanation? One possible answer is that these operations are, under some market circumstances, a more efficient way to sell retail gasoline.

It should be emphasised that only under some conditions will refiner-operated stations be more efficient. Under a variety of other market conditions, the lessee-dealer will be more efficient. There is absolutely no reason to believe that one form of operation is going to die out completely. There will probably always be a demand for both types of stations. To completely eliminate one type by law could cost the consumer by reducing the overall efficiency of the retail marketing system.

CONCLUSIONS

The lessee dealers have claimed that refiners have employed predatory pricing to force retail prices down to a level which has eliminated all of the profits from retail marketing. Unable to withstand these losses, the dealers are being forced from the market. The proponents of divorcement have insisted that this legislation would increase competition in the retail petroleum market and lower prices to the public.

This has to be the strangest argument that I have ever heard. If prices are already so low that there are no profits, and if divorcement increases competition and further lowers prices, surely more dealers will be forced out. Why would dealers claim otherwise? Why do they act surprised when studies of Maryland show that prices increased following divorcement?

The answer is obvious. Divorcement does not lower prices, it raises them. That is why the dealers are supporting the legislation. Using the numbers reported in my Maryland study, if you have divorcement at the Federal level, the average dealer,

located near a divorced station, will be able to raise prices because of the elimination of the low priced competition. This dealer will be able to earn an EXTRA \$7,500 per year from gas sales alone. That is why dealers are supporting this type of legislation.

Of course, someone must pay for these extra dealer earnings. Again, using the numbers from the Maryland study, we can expect the consumers to pay nearly \$1 billion a year more for their gasoline than they are currently paying.

In closing, let me point out that critics will claim many things about my Maryland study. As with any research, there are problems. Most, if not all of these, I have attempted to point out and resolve. For the last 18 months this research project has been under review by other academics in economics and statistics, and by experts in the petroleum industry on both sides of the divorcement issue. After this careful scrutiny, the University of Chicago has decided to publish this study in *The Journal of Law and Economics*, one of the most prestigious journals in its field.

Senator MATHIAS. Mr. Reilly.

STATEMENT OF EDWARD G. REILLY

Mr. REILLY. Thank you, Mr. Chairman.

My name is Edward Reilly. I am vice president of marketing for the Atlantic Richfield Co. I want to thank you and the members of the committee for giving me the opportunity to express our views.

It appears to me that those dealers who are advocating passage of legislation such as S. 40--and I say "those," because I do not think all dealers support that--have one basic charge, and that charge is that the numbers of service station dealers are declining, and the reason that they are declining is that the major refiners--and I usually identify those as the 15 largest majors--through some illegal tactic such as predatory pricing or exorbitant rents or the like, are forcing them out of business and then taking over the station themselves and operating those stations as company operations.

I personally would agree that the divorcement bill is necessary if, in fact, that were true.

I believe, however, that the data which is readily available--and it is not industry data, but government data--clearly indicates that that is not happening.

Back in 1972, the 15 refiners operated about 2 percent of their own service stations, which is to say that somebody else operated the other 98 percent. By 1977, that had gone up to 3 percent; and in 1981, which is the latest data that I have from the Department of Energy, that remained at 3 percent.

So if there is a very significant loss in the number of service station dealers in the United States—and I agree that there are—they certainly have not gone over to company operation by the 15 major refiners.

Now, the population of service stations in the United States has declined. I do not think anyone would argue that. According to government statistics, they have declined from something in the neighborhood of 225,000 back in 1972 to something in the neighborhood of 150,000 today. And I think there are several reasons for that, but three primary ones.

First of all, for the first time in our history, I believe, gasoline demand in the United States has declined. As a matter of fact, from 1977 through today, I would estimate that gasoline demand in the United States has declined some 20 percent.

Second, there have been several new entrants into the service aspect of the service station marketing, and it has very negatively impacted service station dealers. I refer to such entrants as the mass merchandisers—the Sears Roebucks of the world, if you will—and any number of specialty-type shops doing such things as mufflers, brakes, tuneups, and the like. They have very significantly impacted the service work that predominantly was accomplished by the so-called traditional service station dealer.

And the third reason, in my judgment, and perhaps the most important one, is that there has been a marked change in customer and consumer preference. Like it or not, in the United States today, more than 70 percent of all gasoline is sold via the self-serve method. And the reason for that is clear. The consumer is saying that he wants a quality product at the lowest possible price that he can get it for, and that he is willing to trade off some of the services he heretofore got when he fueled his automobile. That has very significantly impacted a good many dealers who worked on relatively high margins and did relatively low volumes. They suffered.

But I think it is important to note that the decline in the service stations dealers has not gone over or increased the number of service stations operated by the major refiner.

So let me conclude—and it will be the first time in my life, Mr. Chairman, that I have ever beaten the green light—

Senator MATHIAS. You are getting more professional—as a witness.

Mr. REILLY. Thank you.

Let me finish, then, by saying that we respectfully request that legislation such as S. 40 be rejected.

I would be happy to answer any questions that you may have—including the one on prices.

Senator MATHIAS. Thank you very much.

[The following was received for the record:]

PRESENTED BY: E. G. REILLY, VICE PRESIDENT
RETAIL MARKETING
ATLANTIC RICHFIELD COMPANY

THE MAJOR PROVISIONS OF THIS BILL, DIVORCEMENT AND OPEN SUPPLY, HAVE TWO COMMON TRAITS. THEY ARE ANTI-COMPETITIVE AND THEY ARE ANTI-CONSUMER IN THEIR RESULTS.

TAKEN IN ORDER, THE FOLLOWING WILL BRIEFLY OUTLINE OUR REASONS SUPPORTING THESE STATEMENTS:

DIVORCEMENT

DIVORCEMENT SIMPLY MEANS ELIMINATING BY THE MEAT CLEAVER METHOD A CLASS OF COMPETITOR FROM THE MARKETPLACE IN SALES OF GASOLINE AT RETAIL. ONLY THE LARGER, INTEGRATED REFINERS ARE SINGLED OUT FOR THIS TREATMENT. THE SMALLER AND NON-INTEGRATED REFINERS AS WELL AS DISTRIBUTORS AND CHAIN RETAILERS, REGARDLESS OF SIZE, ARE STILL FREE TO MARKET GASOLINE AT THE RETAIL LEVEL. BY DEFINITION, THIS CREATES AN ANTI-COMPETITIVE SITUATION BENEFITING SOME REFINERS AND MARKETERS AT THE EXPENSE OF THE LARGER INTEGRATED REFINERS. MOST IMPORTANT, CONSUMERS WILL PAY HIGHER GASOLINE PRICES DUE TO REDUCED COMPETITION IN THE MARKETPLACE.

SUPPORTERS OF DIVORCEMENT LEGISLATION CLAIM THAT REFINERS ARE DRIVING INDEPENDENT DEALERS OUT OF BUSINESS AND CONVERTING THE STATIONS TO COMPANY OPERATIONS THROUGH SUCH TACTICS AS PREDATORY PRICING AND IMPLEMENTING UNFAIR RENTAL PROGRAMS. THIS ALLEGATION IS FALSE.

DOE PUBLISHED STATION COUNTS FOR REFINERS THROUGH SEPTEMBER 1981. THE LUNDBERG COMPANY HAS PUBLISHED STATISTICS FOR THE U.S. SERVICE STATION POPULATION FOR THE YEARS 1972 THROUGH 1982. BASED ON THESE DATA SOURCES THE 15 MAJOR INTEGRATED REFINERS OPERATED:

- 2.1% OF ALL RETAIL SERVICE STATIONS IN 1972;
- 3% OF ALL STATIONS IN 1977;

- AND 3% IN 1981 WHEN DOE CEASED PUBLICATION OF THEIR STATION COUNT STATISTICS.

THIS MEANS THAT SOMEONE ELSE, OTHER THAN THE 15 MAJOR REFINERS, OPERATED ABOUT 97% OF ALL THE SERVICE STATIONS DURING THIS PERIOD OF TIME; CERTAINLY NO EVIDENCE OF A MASSIVE MOVEMENT TO COMPANY OPERATED STATIONS BY THE MAJOR REFINERS.

DOE BEGAN PUBLISHING A NEW REPORT IN JANUARY 1983 WHICH DISPLAYS DATA RELATING TO REFINER OPERATED STATIONS. THE REPORT DOES NOT PROVIDE INFORMATION ON STATION COUNT BUT DOES DISPLAY GASOLINE VOLUME MOVED THROUGH REFINER OPERATED STATIONS. THE LATEST DATA IS THROUGH NOVEMBER 1983 AND INFORMATION FROM (19) REFINERS IS INCORPORATED IN THE MAJOR REFINER CATEGORY. VOLUME SOLD TO COMPANY OPERATED STATIONS FOR THE FIRST ELEVEN MONTHS OF 1983 BY MAJOR REFINERS IS STABLE AND SHOWS NO GROWTH PATTERN. SALES TO COMPANY OPERATED STATIONS IN JANUARY 1983 REPRESENTED 12.5% OF THE MAJOR REFINER'S TOTAL GASOLINE SALES. THE COMPARABLE FIGURE FOR NOVEMBER 1983 WAS 12.7% AND THERE WERE MONTHS WHERE THE PERCENTAGE WAS UNDER 12%. THIS DATA FOR 1983 FURTHER SUBSTANTIATES THAT THERE IS NO EFFORT TO CONVERT LARGE NUMBERS OF INDEPENDENT DEALER STATIONS TO COMPANY OPERATIONS.

OF THE NEARLY 4500 STATIONS FLYING THE ARCO FLAG, ONLY 6% ARE COMPANY OPERATED BY ATLANTIC RICHFIELD. WE ARE NOW, AND HISTORICALLY HAVE BEEN, COMMITTED TO THE INDEPENDENT DEALER MODE OF OPERATION. THIS IS BECAUSE WE ARE CONVINCED THAT OUR DEALERS CAN OPERATE THE MAJORITY OF OUR SERVICE STATIONS BETTER THAN WE CAN.

THERE IS NO QUESTION THAT THE TOTAL NUMBER OF SERVICE STATIONS IN THIS NATION HAS BEEN DECLINING FOR SEVERAL YEARS AND WILL LIKELY CONTINUE TO DECLINE. THE REASONS FOR THIS ARE REDUCED GASOLINE DEMAND AND CHANGING CONSUMER BUYING HABITS.

- MOST MOTORISTS BUY THEIR GASOLINE AT SELF-SERVE FACILITIES FEATURING LOW PRICES.
- MANY NOW HAVE THEIR AUTOMOTIVE SERVICE WORK DONE AT SERVICE SPECIALISTS SUCH AS MIDAS, AAMCO, SEARS AND GOODYEAR.

- CONVENIENCE STORES SELLING GASOLINE AND FOOD ITEMS CONTINUE TO ATTRACT INCREASED NUMBER OF CONSUMERS WITH THEIR ONE-STOP SHOPPING APPEAL.

THESE CONSUMER PREFERENCES ALL HAVE A COMMON THEME, QUALITY GOODS, FAST SERVICE AND LOW PRICES. GASOLINE MARKETERS WHO HAVE CHANGED THEIR BUSINESS PRACTICES, THEIR FACILITIES AND PRICES TO PASS ALONG SAVINGS ACHIEVED THROUGH ECONOMIES OF SCALE, HIGHER VOLUMES AND SELF-SERVE HAVE PROSPERED. THE MARKETERS WHO CAN'T OR WON'T CHANGE IN RESPONSE TO CHANGING CONSUMER DEMANDS HAVE GONE OUT OF BUSINESS OR ARE SEEKING LEGISLATIVE PROTECTION SUCH AS THIS DIVORCEMENT BILL.

THE PROponents OF DIVORCEMENT LEGISLATION WANT TO BE INSULATED FROM THE REALITIES OF THE COMPETITIVE MARKETPLACE. THEY WANT TO MAINTAIN THE STATUS QUO OF HIGH MARGINS, LIMITED CHANGE IN MARKETING METHODS, AND IF POSSIBLE ELIMINATE COMPETITION TO LIMIT THE RANGE OF CONSUMER CHOICES IN THE MARKETPLACE. THEY WANT CONSUMERS TO PAY HIGHER PRICES FOR GASOLINE TO PERPETUATE THEIR BUSINESS METHODS AND INVESTMENTS. THEY DO NOT RECOGNIZE THE CONSUMER'S EXPRESSED DESIRES AND PREFERENCES WHICH ARE SO CLEARLY EVIDENT FROM DATA WHICH DEMONSTRATES THAT CONSUMERS HAVE SHIFTED THE BULK OF THEIR SPENDING TO CONVENIENT, EFFICIENT, LOW PRICE SUPPLIERS OF AUTOMOTIVE SERVICE AND GASOLINE. OVER SEVENTY PERCENT (70%) OF ALL GASOLINE IS NOW PURCHASED AT SELF-SERVE COMPARED TO TWENTY PERCENT (20%) IN 1974. SERVICE STATIONS ENJOYED SEVENTY PERCENT (70%) OF THE MOTOR OIL MARKET IN 1961, BUT ONLY TWENTY FOUR PERCENT (24%) BY 1981.

THESE EXAMPLES, AND THERE ARE MANY OTHERS OF THE SAME TREND, PROVE THAT CONSUMERS DO NOT WANT WHAT THE PROponents OF DIVORCEMENT ARE TRYING TO SELL. WITH OR WITHOUT DIVORCEMENT LEGISLATION, THE NUMBER OF LOW VOLUME, HIGH MARGIN FACILITIES WILL CONTINUE TO DECREASE UNTIL THEIR NUMBERS MATCH THE DEMAND FOR THEIR SERVICES BY THE MOTORING PUBLIC.

THERE IS AN ABUNDANCE OF EVIDENCE THAT DIVORCEMENT RESULTS IN HIGHER PRICES TO CONSUMERS. MARYLAND HAS BOTH A DIVORCEMENT LAW AND A

FORM OF PRICE CONTROLS IN EFFECT. IN JANUARY 1979, (A PRE-DIVORCEMENT MONTH) PUMP PRICES ON AN EX-TAX BASIS IN PHILADELPHIA AND BALTIMORE WERE ALMOST EQUAL; PLUS OR MINUS ONE CENT. BY DECEMBER 1983, FULL-SERVE PRICES WERE 18¢ TO 19¢ HIGHER IN BALTIMORE AND SELF-SERVE PRICES WERE 2¢ TO ALMOST 4¢ HIGHER, DEPENDING ON GRADE. THE EXHIBIT ATTACHED TO THIS TESTIMONY DISPLAYS THIS INFORMATION. CLEARLY, THESE ANTI-COMPETITIVE LAWS HAVE CAUSED MARYLAND CONSUMERS TO PAY SIGNIFICANTLY HIGHER GASOLINE PRICES.

OPEN SUPPLY

THE "OPEN SUPPLY" PROVISION AMOUNTS TO "OVERKILL" SINCE BRANDED RETAILERS CAN PRACTICE "OPEN SUPPLY" TODAY, IF THEY SO DESIRE, WITHOUT S-40. AS A GENERAL RULE THEY DO NOT DO SO BECAUSE THEY KNOW CONSUMERS WILL NOT TRUST NOR BUY "NO BRAND" PRODUCT IN A BRANDED SERVICE STATION. OUR PRODUCTS AGREEMENTS DO NOT CONTAIN ANY EXCLUSIVE DEALING PROVISIONS, BUT DO PROVIDE FOR PROTECTION OF OUR TRADEMARKS.

THE OPEN SUPPLY PROVISION IN THIS BILL WOULD PUT A FEDERAL STAMP OF APPROVAL ON THE DEGRADATION OF THE VALUE OF TRADEMARKS AND BRANDED MOTOR FUELS IN THE MARKETPLACE. OVER SEVENTY PERCENT (70%) OF CONSUMERS ARE WILLING TO PAY A PREMIUM FOR BRANDED GASOLINE -- TO KNOW THEY GET WHAT THEY ARE PAYING FOR. THEY ALSO KNOW THEY HAVE SOMEONE TO FALL BACK ON IF THEY HAVE PROBLEMS WITH A BRANDED PRODUCT -- THE REFINER,

THE REQUIREMENT TO PROVIDE "REASONABLE NOTICE" TO CONSUMERS THAT MOTOR FUELS OFFERED FOR SALE ARE NOT MADE BY THE REFINER WHOSE TRADEMARK IS ADVERTISED CAN ONLY LEAD TO CONFUSION AND CUSTOMER DISTRUST. NO ONE WILL BE CAPABLE OF GUARANTEEING FUEL QUALITY, OCTANE OR LEAD CONTENT IF OPEN SUPPLY IS PUT INTO PRACTICE.

ATLANTIC RICHFIELD URGES THIS COMMITTEE TO REJECT SENATE BILL 40 AS IT IS NOT IN THE BEST INTEREST OF CONSUMERS OR THE INDUSTRY. WE ALSO REQUEST THAT OUR COMPLETE POSITION PAPER ON DIVORCEMENT BE PLACED IN THE RECORD.

**ATLANTIC RICHFIELD COMPANY'S POSITION ON PROPOSED
LEGISLATION MANDATING DIVORCEMENT OF
COMPANY OPERATED SERVICE STATIONS**

A number of bills have been presented to federal and state legislative bodies over the last several years which would require that some or all refiners cease operating company stations. Some of these bills would also prohibit distributors from operating stations with salaried employees. The proponents of such legislation argue that the substantial decline in the number of independent dealer-run stations is due to an increase in refiner-operated stations and the alleged predatory pricing practices of those facilities.

Atlantic Richfield believes these allegations to be ill-founded and opposes such legislation for the following reasons:

THE DECLINE IN THE NUMBER OF STATIONS OPERATED BY INDEPENDENT DEALERS IS THE RESULT OF CHANGES IN CONSUMER BUYING HABITS AND ECONOMIC FACTORS AFFECTING GASOLINE MARKETING.

Radical changes have permanently altered the way gasoline is sold. During the pre-1973 oil embargo period, crude oil was in ample supply, inexpensive and the demand for gasoline was increasing. Oil companies aggressively competed by building thousands of new service stations. A common complaint at that time was there was a station on every corner of major intersections.

Some dealers scratched out only a marginal living in small volume stations relying on repair work to keep them in business. Dealer turnover was high, running 25 percent or more, in many areas of the country.

This scenario was abruptly and irreversibly changed by the Arab oil embargo, the Iranian crisis and the new economic realities ushered in by the series of price increases that followed each.

The cost of crude oil skyrocketed and quickly translated into dramatically higher gasoline prices. Gradually reacting to higher prices, motorists began to conserve and use less gasoline. These efforts were aided by federally mandated mileage standards for new cars. With demand decreasing, competition has become much more intense as marketers battle to increase or maintain market shares in a shrinking market.

Price became the dominant factor to the consumer when making a gasoline purchase. Aggressive marketers recognized the importance of price and offered motorists lower prices through:

1. Self-serve, where lower prices are possible because the station operator has lower overhead costs due to labor savings and economies of scale.
2. "Gas and Go" operations, which generate large volumes. Such facilities offer low prices through self-serve operations and the acceptance of cash only. "Gas and Go" stations are often staffed by one employee whose function is simply to clear pumps by remote control and collect cash.
3. Ancillary businesses, such as convenience food stores, which attract motorists through self-serve prices and the one-stop shopping concept.

4. Mass merchandisers which offer a variety of services and products, including gasoline, at attractive prices. (Examples are retailers such as Sears, Wards and other chain operators.)

The small volume dealer facing growing competition for gasoline volumes also saw his profits from service work eroding. Manufacturers produced cars that require much less service. Specialty shops proliferated, offering every type of service -- from tune-ups to fast oil changes. Mass merchandisers entered the automotive product and service field and have been successful in capturing a significant share of the market. New car agencies, through longer term guarantees and service contracts, siphoned off work that had traditionally gone to stations. This was compounded by the fact that many service station dealers lack the necessary training and sophisticated equipment to cope with the mechanical complexities of new automobiles.

Faced with these competitive factors, many economically marginal stations were forced to close. Higher operating costs for labor, Social Security, real property taxes, and utilities added to the pressures that confronted dealers. To this trend of station closures was added another trend -- a sharp decline in the number of stations being built. Suppliers found it difficult to justify new construction because of inflationary land and building costs. Since independent dealers comprise the majority of those parties operating service stations, they suffered the largest decline in number.

Finally, the adverse impact that the allocation and price regulations had on the independent dealers was all too apparent. It was virtually impossible for an existing dealer, especially a major brand dealer, to secure an increase in allocation from the Department of Energy. Other marketers, primarily distributors, however, could reopen closed stations or install pumps in front of other types of outlets and often secure huge entitlements from the DOE under their "New Station" procedures. Price controls often favored one competitor versus another, and thwarted a refiner's efforts to keep his dealers competitive. As a result, many major brand dealers left the business during the more than seven years that controls remained in effect.

The trend toward fewer service stations has continued since the termination of controls and a return to a free and competitive gasoline marketplace. The decline in the number of dealer-operated service stations is, therefore, the direct result of changes in consumer buying habits, economic factors and government regulation. Prohibiting refiners from operating stations will not alter or reverse these market trends.

ENACTMENT OF LEGISLATION REQUIRING DIVORCEMENT OF REFINER-OPERATED STATIONS IS NOT BENEFICIAL TO CONSUMERS.

Divorcement removes a competitive force from the marketplace. This type of special interest legislation is designed to benefit a small number of individual dealers. However, the consumer suffers when such legislation is enacted.

Antitrust laws were designed to increase, not inhibit, competition. Refiner-operated stations are, generally speaking, conveniently located, attractively designed facilities that feature such modern marketing techniques as self-serve operations which sell gasoline at competitive prices. Many are open 24 hours a day.

Consumers are best protected by markets in which multiple suppliers are allowed to compete for their business. Legisla-

tion mandating that a refiner cannot sell at retail is like saying that a farmer cannot operate a roadside stand because such an operation might provide unfair competition for a nearby small grocery store. When legislation is enacted that reduces or restricts the number or type of competitors, the consumer is invariably beset with higher prices.

A study by John Barron and John Umbeck, both professors at Purdue University, on the effects of divorcement in Maryland since 1979 document this anti-consumer impact. See the attached Exhibit "A" which summarizes their study findings on the results of divorcement.

Maryland also passed an anti-competitive statewide uniform pricing law. What resulted is clearly shown in attached Exhibit "B" depicting the difference in pump prices between the Philadelphia and Baltimore metropolitan areas on an ex-tax basis. Self-serve prices in Philadelphia were 2¢ to 4¢ less than Baltimore in December, 1983, depending on grade, while full serve prices were an astounding 18¢ to 19¢ less in Philadelphia.

The elimination of refiner operated stations through legislation produces other unfortunate side effects as well. These facilities are operated by salaried employees. Many of these employees will find themselves unemployed if refiner operated facilities no longer exist. Even if an independent dealer should take over the facility, there is no guarantee he would retain the employees. With unemployment rates as high as they are, it might be difficult for these people to find other employment.

Some of these facilities may close permanently since potential independent dealers often do not have the capital to purchase locations that refiners decide to sell. Furthermore, although new construction is limited, companies would be reluctant to build new stations if faced with divorcement legislation since such laws produce a poor investment climate.

THERE IS NO RATIONALE TO SUPPORT THE VIEW THAT MAJOR REFINERS WILL DRIVE THEIR OWN INDEPENDENT DEALERS OUT OF BUSINESS.

Major refiners have a huge investment in marketing assets operated by their branded independent dealers. It would make absolutely no sense for a refiner to take any action that would damage its network of independent dealers. Any such action that weakened its branded dealer operation would only serve to undermine the refiner's competitive position and thereby reduce its profits.

Proponents claim that divorcement legislation is required since refiners engage in predatory pricing through their company operated stations to the detriment of their independent dealers. Atlantic Richfield can only speak to its own operations. ARCO company operated stations are run by a subsidiary company. The facilities operated by the subsidiary company are leased from Atlantic Richfield on the same terms as those leased by ARCO independent dealers. Company operated facilities and ARCO independent dealers supplied by Atlantic Richfield that are located in the same geographic area pay the same price for ARCO gasoline. Therefore, these company operated stations can only be a "threat" in the sense that if they are more efficient, they may then be able to offer consumers lower prices.

Stations operated by major refiners also provide benefits to the entire dealer organization. One way this is done is through their use to test new techniques. Such experiments are often too expensive or risky to be tested by an individual dealer. Once programs being tested prove successful, refiners

make them available to their dealers. In addition, company operated stations provide refiners with first hand information about how the market works. This knowledge is imperative in today's intensively competitive, rapidly changing marketplace.

But beyond this, considering the number of refiner-operated stations, the degree of concern expressed by some about the role of major refiners is totally without merit, as the following statistics furnished by the DOE clearly show:

	<u>Average Number of Refiner Operated Service Stations during</u>		
	<u>12 Mos. 1972</u>	<u>12 Mos. 1977</u>	<u>9 Mos. 1981*</u>
15 Major Refiners	5,917	6,805	5,761
All Other Refiners	<u>5,336</u>	<u>8,851</u>	<u>7,099</u>
Total	11,253	15,656	12,860

(*The last period the DOE compiled these statistics.)

Major refiners (the fifteen largest per DOE definition) decreased by 156 units the number of directly-operated stations during the period. Other refiners, who generally operate in smaller geographic areas, increased their portfolio of such stations by 1,763. The Lundberg Company has published statistics for the U. S. service station population for the years 1972 through 1982. Based on the Lundberg data and the DOE service station count statistics, the 15 major integrated refiners operated:

- o 2.1% of all retail service stations in 1972.
- o 3% of all stations in 1977.
- o and 3% in 1981 when DOE ceased publication of their station count statistics

This means that someone else other than the 15 major refiners operated about 97% of all the service stations during this period of time; certainly no evidence of a massive movement to company operated stations by the major refiners.

Many prominent government bodies have rejected the concept of divorcement. Both the Department of Justice and the Department of Energy have recommended against bills that would force major refiners to cease operating company stations. The Department of Justice has taken the position that such laws should only be enacted if there is a serious failure on the part of the free market to allocate goods and services. They have found there is no evidence to support such a conclusion.

Furthermore, there is already a body of law in effect that protects dealers. These include (1) the antitrust laws and (2) the Petroleum Marketing Practices Act which prohibits arbitrary lease cancellation and non-renewals.

State legislatures have also overwhelmingly rejected retail divorcement bills. Since 1974, legislation dealing with retail divorcement was introduced 178 times. Only five states have enacted such laws. These are Connecticut, District of Columbia, Delaware, Maryland and Virginia. (Florida enacted legislation in 1974, but it has since been repealed.) The United States Congress has considered divorcement legislation regularly since the 95th Congress in 1978 with no affirmative result to date.

CONCLUSION

Divorcement legislation reflects the view that dealers are threatened with extinction, particularly by major refiners. This is not true.

The retail sector is indeed changing, but we believe these changes are the normal result of competitive factors and economic conditions that affect all marketers. Independent dealers can survive in a changed environment. Divorcement legislation focuses on casualties of change and overlooks the experience of many independent dealers who have adapted successfully to changing conditions in the marketplace. An example of this is contained in the July, 1983 National Petroleum News article, attached as Exhibit "C". Moreover, it fails to consider the likelihood that a significant portion of consumers will continue to seek the extra services which dealers have historically provided. The entire refining and marketing segment of the petroleum industry is undergoing fundamental changes. Divorcement legislation attempts to selectively minimize the impact of this change and to prevent the necessary and inevitable adjustments that a free and vital market requires.

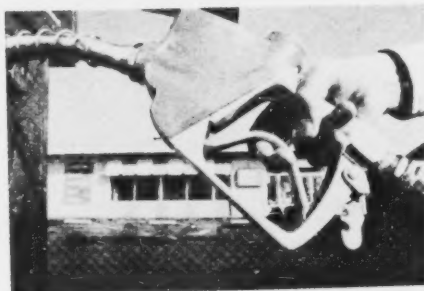
Divorcement bills should be rejected. Such an outcome in our opinion would be good not only for dealers, jobbers and refiners, but primarily for the American consumer.

The Maryland Divorcement Experience Updated:

A Summary By
John M. Barron and John R. Umbeck
Professors of Economics
Purdue University

The state of Maryland enacted divorcement legislation which, effective July, 1979, prevented refiners from operating retail gasoline service stations in that state. Because of the potential impact of this "divorcement" legislation, Professor John Barron and I conducted a research project measuring the effects of divorcement legislation in the state of Maryland. This study was undertaken in the fall of 1981 and was underwritten by the Committee of Independent Refiner Marketers.

The study clearly revealed that the legally forced franchising of company operated stations in Maryland had several negative impacts, including higher gasoline prices at stations directly affected by the law, higher gasoline prices at immediate competitors, shorter station hours, and a decline in the number of service stations in operation within the state. In November and December, 1982, we undertook an extensive update of our original research. That update has been underwritten by the Atlantic Richfield Company. As was the case with the original study, control of all phases of the study, from design through analysis, remained with the authors. This report summarizes the latest findings. For those interested in reviewing the technical details, a copy of the complete study is available upon request.



Conclusions

After updating our original study we conclude that our earlier results still hold. Maryland's divorce legislation has caused retail gasoline prices to increase not only at stations directly affected by the law but also at nearby competitors. The new updated study further substantiates that the legislation has led to fewer service stations being available to Maryland motorists and shorter hours of operation at many remaining stations.

The updated study relied upon a different data source (the Lundberg organization) than the original study (refiner supplied information) and included a substantial validation of the data provided by that independent source. The consistency of the findings of the two studies provides further substantiation of the accuracy of the conclusions. Allegations of possible data bias, while certainly a potential problem in any economic experiment, do not appear to affect this particular study of the Maryland divorce experience. Each of our tests, direct and indirect, revealed at each stage no evidence of error (either deliberate or accidental) in the data.



Study Detail

Original Project Design

In our original study, we contacted representatives from each oil company which operated stations directly affected by divorce legislation. Each received a questionnaire requesting information on all of their company-operated stations and their nearby competitor's stations. We asked for information on retail prices for each grade of gasoline and each type of service over a five year period before and after divorce took place. We also collected data on the different types of services offered at each station and the hours they remained open each week. Armed with this data, we isolated and measured the actual effects of the divorce law and we constructed a detailed picture of about 150 local Maryland gasoline markets. Each market contained one gas station which was legally forced to divorce and four or five nearby competitors. Within these local markets we tracked each station's retail prices of gasoline sold, both self and full serve, and all grades available. These prices covered a period before and after the date of divorce for each company-operated station. Utilizing this technique, we separated out the effects of deregulation, crude oil price changes, declining aggregate demand for gasoline, and so on. All that remained was the effect of legal divorce.

Over the last year, this study has been carefully examined by experts in a variety of fields including professional statisticians at an academic journal, researchers at the American Petroleum Institute, state and national gasoline dealer associations, legislators and governmental research teams. The study has encountered only one significant criticism: a possible bias in the data because all of our information was provided by the oil companies which were affected by divorce. These companies may have had an incentive to deliberately distort the data to make it appear that divorce led to higher prices and less consumer service. If companies could successfully create this impression, the critics said, perhaps similar legislation would not be passed elsewhere. Of course, this concern is legitimate. As any economist knows, individuals always have incentives to bias data in their own self interest; oil companies are no exception. In anticipation of this, we had built into the original study a number of checks for possible data bias and, while we found no evidence of any distortions, it was still possible that some incorrect information was given to us. The opportunity to update the original study in the fall of 1982 provided the means to check the accuracy of the original data even further.

New Project Design

The services of Mr. Dan Lundberg, a well known petroleum market price observer, were employed to re-survey the entire sample from the original study. None of the oil companies was notified of the re-survey. Over a three-day period, all the prices at all the pumps from all the stations in the sample were collected along with information on the geographic location of each station and the types of services provided. To further guarantee the integrity of the information, I employed an economist from the University of Delaware to randomly re-survey a portion of the stations surveyed by Mr. Lundberg's survey team. No one, including myself, knew which stations would be checked. The Lundberg data was determined to be completely accurate when compared with the re-survey results.

The new and independently verified data was then analyzed using a statistical technique known as multiple regression analysis. This procedure allows us to account for the effect of a number of variables other than divorcement on the retail price. In this fashion, we were able to detect the effects on retail gas prices of the number of pumps and hoses at each station, credit cards, cash discounts, self and full serve, service bays, convenience stores, and so on.

The first test with the new data was to reproduce our original study with the new information included to see if our original results were still valid. *Our findings confirmed our earlier conclusions. Divorcement legislation in Maryland caused a significant increase in retail gasoline prices* at those stations directly affected by the law and at their nearby competitors. In particular, a typical company-operated station before divorcement was selling regular and unleaded gasoline self-serve for 2.32 cents per gallon less than their local competitors. The same station was selling full-serve gasoline for 2.97 cents per gallon less than their competitors. After divorcement, the newly franchised stations (formerly company-operated) raised their prices on average 3.08 cents per gallon on self-serve and 6.26 cents per gallon on full-serve. During the same period, the local competitor stations increased their prices for regular and unleaded gasoline an average of .86 cents per gallon on self-serve and 3.14 cents per gallon on full-serve. In addition, 11 percent of the stations required to be divorced closed after the legal deadline date of July, 1979. About half of these were still closed at the end of 1982. Furthermore, divorced stations which continued in operation under a new franchise contract, were open 8 hours less per week after divorcement.

Detailed New Project Results

The new data provided two additional tests which are of interest. First, it provided additional price information for the year 1982, beyond that contained in the original study. When we added this new data to our original sample and tested for the effects of divorcement, we found no significant differences from our original conclusion that *legally forced divorcement led to higher retail gasoline prices in Maryland*.

The second test used the exact geographic location of each station to check for the data bias which was mentioned earlier. Now that we knew the address of each station we discovered that in several cases a divorced station reported the prices from a competitor which was either another divorced station or a competitor of another divorced station. What this means is that two different oil companies were reporting prices on the same station. This overlap in reported prices allowed for two independent tests for data bias. The first test used the overlap created when one divorced station reported as a competitor the prices of another divorced station owned by another oil company. When this occurred, we discarded the prices at the first divorced station which were collected by the company which owned it and used instead the prices at that station which were reported by its competitor. If the refiner which owned the divorced station had "cheated" or biased the reported prices it would show up in the new test. The results of this test showed only minor differences from the original results. This suggests that even if we throw out all of the prices at the divorced station which were collected by the refiner which owns that station, and substitute prices collected by their competitors, our results will be the same. *The bottom line is this test revealed no data bias*.

The second test is less subtle and much more direct. When an overlap in data reporting occurred, we plotted the prices at the overlap station. Since we had two refiners reporting prices at the same station, any bias would create a difference in the reported price on any given date. This procedure was followed for each overlapping station. *We found no significant differences in the prices reported and no evidence of any data bias*.

Additional Data Verification

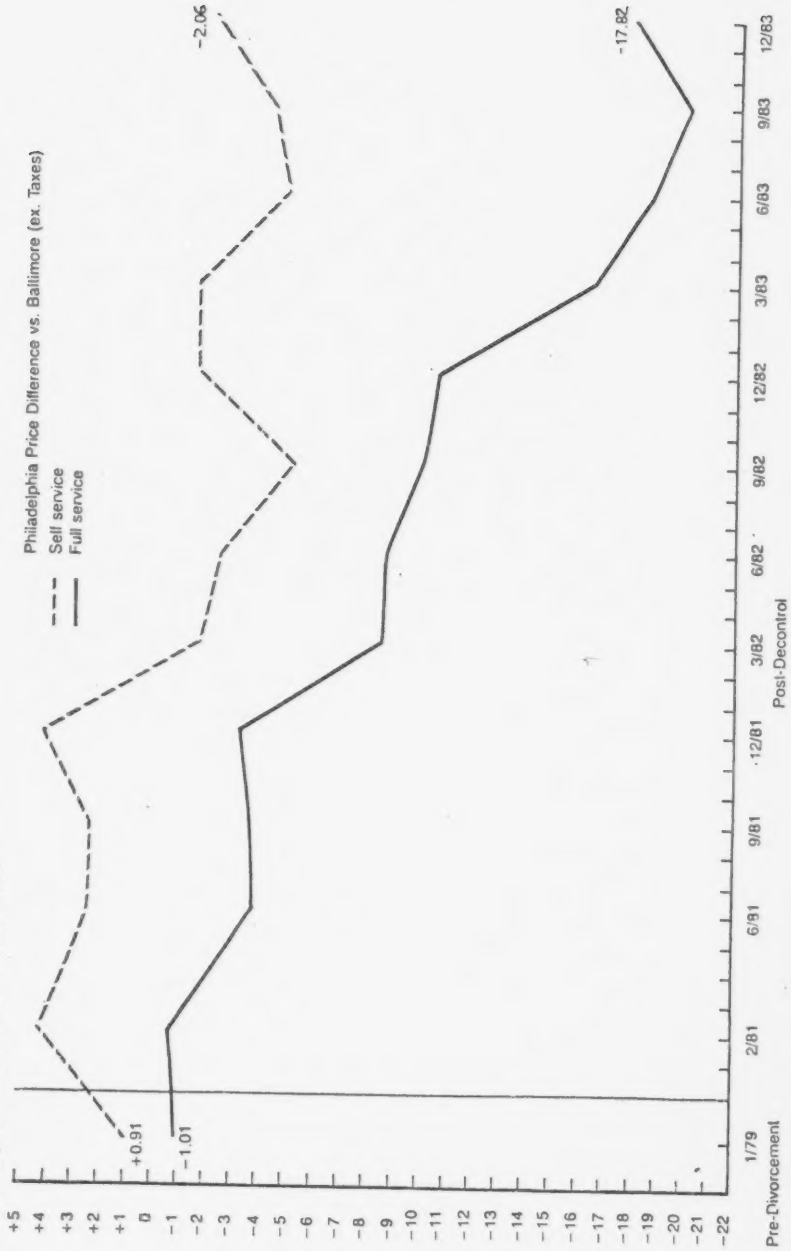
The updated study of the Maryland divorcee experience, summarized herein, provided an external validation of the original study's data base by using a second source for price data not subject to the potential bias to which the oil company data may have been subject. Although the updated study produced substantial assurances of the accuracy of the data, it did not *directly* provide a verification of the accuracy of price data for the period *prior* to the implementation of divorcee.

Because of concerns with this lack of a direct verification, an additional check was conducted to provide such a verification. Historic price data obtained from the Lundberg organization was compared to the data used in my original study and the update to that study. Two different Lundberg surveys were purchased—an October, 1978, census of all Maryland service stations and their prices; ten Baltimore price surveys distributed over the period July, 1977, through October, 1981.

When comparisons were made between the Lundberg prices and the prices originally provided by the oil companies, *no evidence of any bias or cheating in the original data was found*. A total of 352 of the original sample of 600 stations were matched to the October, 1978, Lundberg census. Of these two sets of prices, more than 70 percent matched perfectly. The remainder included errors, but the errors were evenly distributed in both directions, and of minimal magnitude, ruling out any bias. Forty-one of the original 600 stations were included in the regular Lundberg Baltimore price surveys. Lundberg's prices for each of the 41 stations were compared with the original price data provided by the oil companies. These comparisons were conducted in 10 separate months during the period July, 1977, through October, 1981. In all, a total of 410 price pairings were compared. *All* comparisons were within acceptable limits.

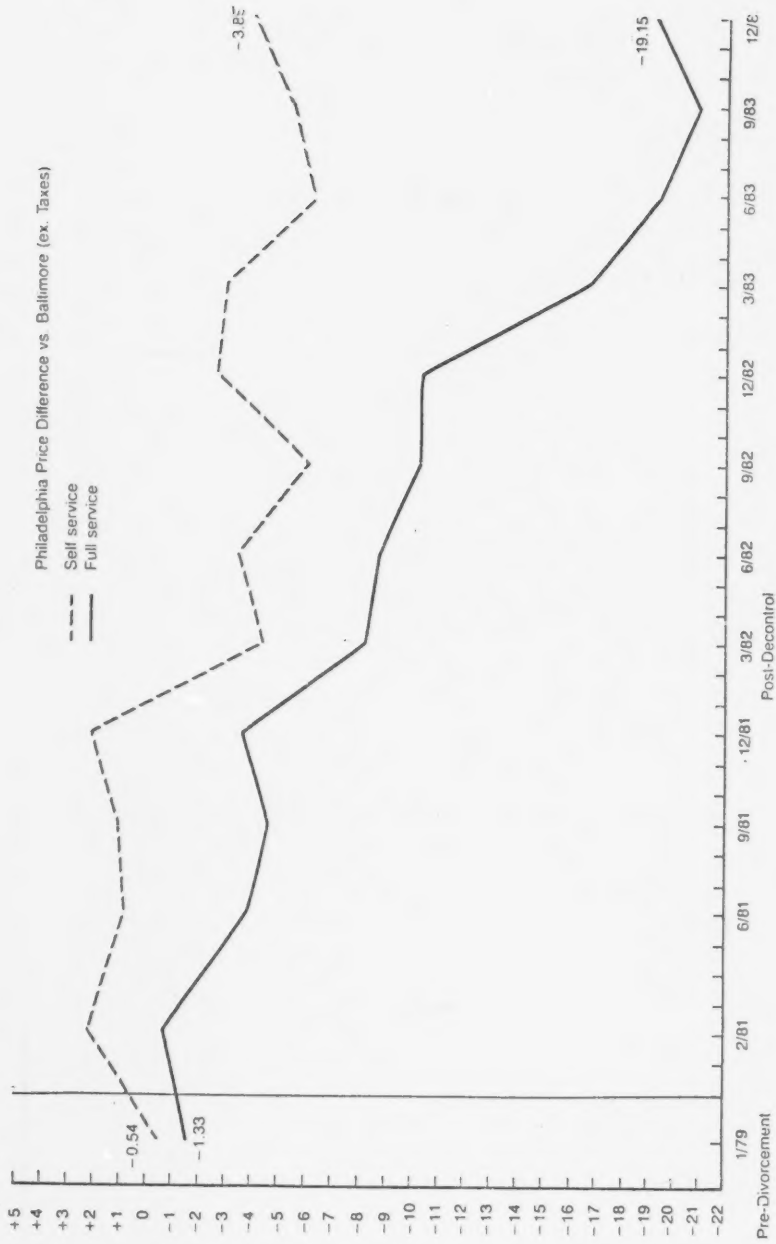
These two checks upon the pre-divorcee price data provide even stronger evidence that no bias or cheating is contained in the data. When combined with earlier data verification, it is clear that the findings of both the original Maryland study and the update to that study are based upon accurate, non-biased information.

Leaded Regular Gasoline
Industry Retail Pump Prices Differences Since Maryland Divorcement/Uniform Pricing Legislation
Philadelphia Metro vs. Baltimore Metro

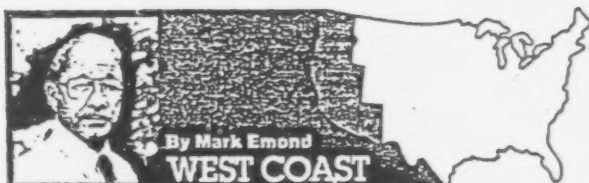


Source: Lundberg Inc. Price Surveys

Unleaded Regular Gasoline
Industry Retail Pump Prices Differences Since Maryland Divorcement/Uniform Pricing Legislation
Philadelphia Metro vs. Baltimore Metro



Source: Lundberg Inc. Price Surveys



Competing Dealers Can't Find Dissent Among Arco's High-Volume Retailers



The am/pm mini-market (and the MP&G tuneup) outlets seem to epitomize the success of the Arco program.

While it was ordained that Atlantic Richfield's cash-only gasoline marketing program would not satisfy all types of its distributors, enough of them seem to be pacified to divine the company's plan a success.

After Arco dropped the credit card more than a year ago, reaction even inside the marketing organization was cautious. And, company dealers were nervous about the selling pressures involved in high-volume, low-price strategies.

Over time, however, gasoline volumes doubled and tripled. The plan, indeed, was working, and many Arco dealers' complaining began to ebb silent.

Outside Arco, competing dealers were losing volume and being crunched in price wars often sustained (if not started) by Arco outlets. One band of independents finally decided to beat the bushes for disgruntled Arco dealers to support their cause.

Serve Yourself and Multiple Pump Assn. (SYMPA), Los Angeles, pitched publicly for Arco dealer disaffection. The group ran newspaper advertisements in several cities, mostly California—Sacramento, San Francisco, Stockton, Fresno, Modesto, San Diego, and Las Vegas.

"Write us about your problems with Arco in full confidence," the ads said. SYMPA hoped to gather evidence of alleged "pressuring" and "threatening" by management reps.

Results were underwhelming. SYMPA had expected "sacks full" of letters. After about a month, the group had received 35, and half were unsigned. Some came from the Pacific Northwest where SYMPA had not advertised. Lawyers weren't sure they had a single case.

There was a pattern of complaints about alleged threats to withhold competitive allowances if dealers wouldn't cut their prices. That would be illegal, of course. These had to be checked out. Paul Erdos, SYMPA's executive director, was hopeful a case could be developed, but not optimistic.

One complaint was interesting. Gasoline volumes had tripled, but margins had shrunk to a third, some said. There was more work, more manpower taken away from the service bays, more driveoffs, but no more money. Not everybody would find fault with triple volume, whatever adjustments it might take.

Significantly, not a single complaint came from dealers operating am/pm mini-markets. It is this type of Arco retailer that perhaps epitomizes the success of Arco's program from their point of view.

Except perhaps for some high-volume MP&G tuneup centers which came much later, am/pm outlets have been recognized as some of the toughest competitors on the street. Many were getting big temporary competitive allowances enabling them to overwhelm competitors at the cost of shaving margins to the bone.

There can be no doubt that it was the am/pm stations that carried Arco's war to the streets. They were the assault force Arco depended on to establish the pitch of price competition and to amass the necessary volume that would be the fundamental measure of the program's success.

The am/pm operators bore the brunt of the company's will, and they potentially would have been protest leaders if the program were not working. The am/pm operators are, quite the contrary, mute but eloquent evidence that Arco's program is good business for them.

EXHIBIT "C"

Look at the am/pm record. The 750 am/pm mini-markets planned to be in operation by the end of 1983 are officially forecast to record \$300-million in food sales—an average of \$400,000 a year, or \$33,333 a month.

Trade sources consider a profit margin of 25% reasonable, netting an average of \$8,333 a month, or \$100,000 a year. (Arco's 11% royalty on that \$300-million is \$33-million.)

On the petroleum side, average monthly gasoline sales of am/pm units officially are forecast to exceed 175,000 gal. by the end of the year. If one figures only 2¢ to 3¢ gal. margin, that's another \$3,500 to \$5,250 a month, or \$42,000 to \$63,000 annually to brighten the picture.

This is not the stuff of which protests are made.

In the rush of independents to switch some private-brand stations to major brands, those who additionally bought an am/pm franchise are probably counting their blessings. One says his whole branded/unbranded retail operation, in the face of disastrous gasoline margins, is being carried by two good am/pm's.

With a franchise fee of \$20,000 in the West and \$15,000 in the East, the am/pm franchise would appear to be a case of almost instant payout.

Arco reports its MP&G tuneup centers hold promise of being even bigger gasoline-volume successes than the am/pm stores. A few months after about 60 MP&G units were opened in the Los Angeles area, Arco said they showed higher gains than the am/pm's or conventional stations [NPN—Feb. '83, p46].

Each MP&G center is a total self-serve operation with a small snack-shop facility featuring high-gross-profit food and drink items. Think of the potential of such a shop with foot traffic of 20,000 gasoline customers a month.

Arco hopes to have 500 MP&G tuneup centers in operation by 1985, about 15% of the number of its current lessee and contract dealers. The company's 750 am/pm markets represent about one-fourth the number of lessee and contract dealers.

In assembling two of the largest chains of ancillary businesses in the country—mini-markets and tuneup centers—Arco is rapidly approaching the day when these diversified franchise operations will exceed 50% of its national chain, not to mention other possible types.

Senator MATHIAS. Mr. Chisholm.

STATEMENT OF PHILLIP R. CHISHOLM

Mr. CHISHOLM. Mr. Chairman, my name is Phil Chisholm. I am executive vice president of the National Oil Jobbers Council.

NOJC is a federation of 42 State and regional marketer associations that represent some 11,000 independent, small business petroleum marketers. We estimate our members sell somewhere in the neighborhood of 50 percent of the gasoline and 85 percent of the home heating oil sold in the country today.

We appreciate the opportunity to be here to testify on S. 40, a bill which, among other things, would prohibit the largest refiners from operating retail service stations. We have been in this posture before, and we have testified on this issue many, many times. Each time we are asked to testify on this particular issue, we again review the motor fuel marketplace, and our position, and see whether either have changed.

After doing that for this particular occasion, we again must conclude that we do not believe retail divorcement is an adequate remedy to many of the problems that independent marketers are now facing.

A review of the domestic motor fuel marketplace will show that it is a highly-competitive and volatile environment. The high degree of competition is something independent motor fuel marketers do not fear; they, in fact, relish that high level of competition, because they believe they are the most efficient gasoline marketers in the country. They are convinced that so long as they and each of their competitors begin at the same starting point, that they will be able to offer the consumer the lowest possible price for motor fuel. They are therefore reluctant to support any legislation prohibiting anyone from the marketplace.

This is not to say that all is well in the motor fuel market. To the contrary—during the past 2 years, independent marketers have been the victims of anticompetitive supplier practices. The nature of these problems, however, differs from one section of the country to the next, depending on a number of different factors. If the problem which independent marketers faced was merely unfair retail competition from outlets operated by the largest of the integrated refiners, then the solution offered by a Federal divorcement statute might seem to be the appropriate answer.

From our perspective, however, we do not see this problem as so overwhelming a national problem as to necessitate a broad divorcement statute. This would seem to be a broadbrush approach to what tends to be differing regional and localized problems.

While there may be some refiners who are attempting to gain market share or gain better control over the refinery output by channeling greater amounts of product through direct-operated outlets, others have attempted to accomplish the same ends via the directly supplied dealer network. In essence, not all refiners are guilty of the same predatory actions that seem to be the basis for this legislation.

We have worked with our member associations, and we feel that in some instances, retail divorcement may be a justifiable remedy

at a State level. And in fact, in some instances, some of our States have endorsed retail divorcement. But we have warned that only in instances where the problem you are trying to address is predatory actions by refiner direct-operated stations is retail divorcement an adequate solution.

On a national level, the problems faced by independent marketers are much greater. They include threats by refiners to terminate marketers for their failure to purchase minimum contractual volumes, even though there is no obligation by the refiner to offer those minimum volumes at a competitive price; threats by refiners to force their customers to accept new contract terms which are harmful to the customer's interests; imposition of unfair trade practices and refiner pricing among various classes of customers; and a concerted effort by refiners to shift the competitive consequences of their pricing actions to their wholesale consumers.

We do not feel that refiner divorcement is an adequate solution to any of these problems. We have worked with the service station dealers. We have come up with what we think is a better solution to many of these problems, and that has recently been embodied in legislation which has been introduced on the House side by Representatives Mike Synar and Tom Tauke, H.R. 5023. I have summarized the essence of that bill in my prepared testimony and would be glad to respond to any questions members of the Subcommittee may have.

Senator MATHIAS. Thank you very much.

[The following was received for the record:]

STATEMENT OF PHILLIP R. CHISHOLMON BEHALF OF THENATIONAL OIL JOBBERS COUNCILPREFACE

The National Oil Jobbers Council is a federation of 42 state and regional trade associations representing thousands of independent small business petroleum marketers. Members include gasoline and diesel fuel wholesalers, commissioned distributors of gasoline, gasoline reseller-retailers and a large number of retail fuel oil dealers. Members also wholesale or retail many other petroleum products, including kerosene, LP gas, aviation fuels and motor oils as well as residual fuel oil. Together our members market approximately 50 percent of the gasoline and 85 percent of the home heating oils sold in America under either their own private brand or the trademark of their supplier.

Mr. Chairman and Members of the Subcommittee:

My name is Phillip R. Chisholm. I am Executive Vice President of the National Oil Jobbers Council (NOJC). NOJC is a federation of 42 regional and state marketer associations which represents some 11,000 independent, small business petroleum products marketing companies. Collectively these companies sell nearly 50 percent of the motor gasoline and 85 percent of the home heating oil marketed in the United States each year.

We sincerely appreciate this opportunity to appear before the Subcommittee to testify regarding S. 40, a bill which would prohibit the largest refiners from operating retail service stations. This issue has been the subject of hearings in past years. At those times NOJC voiced its opposition to retail marketing divorcement at the federal level and its opposition to several other features of the legislation. Each time we prepare our testimony on this issue we review the status of the motor fuels marketplace to determine how passage might affect the problems faced by our small business members. Again this year we have reviewed our position on the concept of federal divorcement.

MOTOR FUELS MARKETING AND RETAIL DIVORCEMENT:

The domestic motor fuels marketplace is a highly competitive and volatile environment. This high degree of competition is something independent motor fuels marketers do not fear. They, in fact, relish it because they believe, with a considerable degree of justification, that they are the most efficient gasoline marketers in the nation. They are convinced that so long as they and each of their competitors begin at the same starting point, they will be able to offer the consumer the lowest possible price for motor fuel. They are, therefore, reluctant to support any legislation prohibiting anyone from the marketplace.

This is not to say that all is well in motor fuels marketing. To the contrary, during the past two years independent marketers have often been the victims of anticompetitive supplier practices. The nature of these problems, however, differs from one section of the country to the next, depending on a number of different factors such as population density, number of suppliers, number of independent marketers, etc.

If the problem which marketers faced was merely unfair retail competition from outlets operated by the largest of integrated refiners, the solution offered by a federal divorcement statute might seem to be the appropriate answer. From our perspective, however, we do not see this problem as so overwhelming a national problem to necessitate a federal divorcement statute. This would seem to be a "broad brush" approach to what tends to be differing regional and localized problems.

While there are some refiners who are attempting to gain marketshare or to gain better "control" over their refinery output by channeling greater amounts of product through direct-operated outlets, others have attempted to accomplish the same ends via their directly-supplied dealer network. In essence, not all refiners are guilty of the same predatory actions that seem to be the basis for this legislation.

Since at this time direct-operated stations appear to be a local or regional problem, NOJC has opted to work with our 42 regional and state associations. We feel a case can be made for divorcement in some states and some of our member associations have supported divorcement in those states. We have warned our members, however, against blindly endorsing divorcement as an emotional response to various and sundry marketer problems. Divorcement should only be supported if the problem in that state is purely anticompetitive actions by refiner-direct operated stations.

On a national level the problems faced by independent marketers are much greater. They include:

- Threats by refiners to terminate marketers for their failure to purchase minimum contractual volumes even though there is no obligation on the refiner to offer those minimum volumes at a competitive price;
- Threats by refiners to force their customers to accept new contract terms which are harmful to the customers' interests;
- Imposition of unfair trade practices in refiner pricing among various classes of customers; and
- A concerted effort by refiners to shift the competitive consequences of their pricing actions to their wholesale customers.

We do not feel that refiner divorcement is an adequate solution to any of these problems. In attempting to design a solution to these problems, NOJC has worked with the Service Station Dealers of America (SSDA) to develop legislation which addresses the chronic problems faced by jobbers and dealers alike. These efforts have been successful. Collectively we have identified solutions to several problems faced by members of both groups. We believe that many of these problems can be addressed by amending the Petroleum Marketing Practices Act (PMPA).

PETROLEUM MARKETING PRACTICES ACT

The Petroleum Marketing Practices Act (PMPA) was enacted in 1978 after several years of debate. In its final form, the bill was essentially franchise protection legislation. It was designed to prevent franchisors (refiners and distributors) from arbitrarily terminating or nonrenewing the franchise relationship with franchisees (distributors and dealers).

The term "franchise" is defined in terms of a motor fuel trademark license owned or controlled by a refiner. Leases of real property and motor fuel supply agreements are also incorporated in the definition of a franchise.

The Act spells out conditions under which termination or nonrenewal are permissible and the steps which a franchisor must take either to effect a termination or a decision to nonrenew the franchise relationship (i.e. cause, notification, etc.). In instances where a franchisee feels that a franchisor has failed to comply with the Act, he may bring a civil action against the franchisor. The courts are authorized to grant equitable relief necessary to remedy the violation. A preliminary injunction is to be granted if the franchisee can demonstrate the existence of sufficiently serious questions, going to the merits, to make them a fair grounds for litigation; and the court determines that balancing of the hardship indicates that the hardship suffered by the franchisee if the injunction were not granted would be greater than the hardship imposed on the franchisor by issuance of such relief.

Regarding terminations and nonrenewals, the PHPA also contains preemption of state law unless the law is "the same as" the applicable provisions of the federal statute.

The Act does not address the issue of the interrelationship of price as a function of supply. On several occasions during the legislative history language was debated relating to predatory pricing policies. The original legislation contained a Title III which prohibited subsidization of downstream operations with upstream profits. That provision was dropped in the House Committee markup, but was retained in a modified version by the Senate Energy Committee. The full Senate deleted Title III and substituted in its place a study of the problem by the Department of Energy.

Clearly, while final language was never approved, the interlinking of price and supply is not a new concept within the parameters of the Petroleum Marketing Practices Act.

Within the last ten days, Representatives Mike Synar (D-OK) and Tom Tauke (R-IA), along with several of their colleagues, have introduced H.R. 5023, the Petroleum Marketing Practices Act Amendments of 1984, which seek to correct many of the unfair practices from which jobbers and dealers have suffered.

I have attached, as Exhibit A, the language of H.R. 5023. In brief, however, the bill does several things:

- It prohibits franchisors from terminating franchisees for failure to purchase minimum gallons unless the franchisor can show it offered those volumes at a competitive price;
- It prohibits franchisors from discriminating in price and allocation policies between its classes for franchisees;
- It provides that in the event of market withdrawal, refiner franchisors must offer franchisees the right of first refusal to purchase the leased marketing premises;
- It requires that changes made in the franchise agreement at the time of renewal be fair and reasonable;
- It prohibits station conversions during the term of the franchise agreement;
- It allows franchisees to continue operating the leased marketing premises in cases where the underlying lease had expired and where the franchisee had been able to negotiate his own agreement with the owner of the property;
- It prohibits franchisors from engaging in anticompetitive pricing practices in instances where they are in competition with their franchisors;
- It allows the courts to approve payment of attorney's fees to the franchisee if it wins final equitable relief, even through actual damages may not be awarded;

- It allows for the sale or transfer of a franchise agreement and allows for the succession of a franchisee under a plan to be approved by the franchisor.

SUMMARY:

We appreciate the efforts of the Chairman to hear from the independent marketing segment of the petroleum industry. While S. 40 is not what we would consider the appropriate remedy at the federal level, many of our state groups are actively pursuing the retail divorcement strategy where it is warranted. We firmly believe that a better alternative is to amend the PMPA so that jobbers and dealers would be afforded a fair and reasonable opportunity to compete based on efficiency, not on size alone. Penalizing a company by removing it from marketing merely because of its size may well create more disruption in the marketplace than it would resolve.

For these reasons NOJC has endorsed and strongly supports the actions of Congressmen Synar and Tauke in introducing H.R. 5023. We believe it singles out those actions which are most onerous to independent marketers and applies a fair and attainable standard for franchisors in their dealings with their franchisees. We commend this language to the Subcommittee in lieu of a federal statute calling for retail marketing divorcement.

MEMBERS OF THE NATIONAL OIL JOBBERS COUNCIL

NOJC represents these member associations:

Alabama Petroleum Marketers Association
 Arizona Oil Marketers Association
 Arkansas Oil Marketers Association, Inc.
 California Independent Oil Marketers Association
 Colorado Petroleum Marketers Association
 Independent Connecticut Petroleum Association
 Florida Petroleum Marketers Association
 Georgia Oilmen's Association
 Idaho Oil Marketers Association
 Illinois Petroleum Marketers Association
 Indiana Oil Marketers Association, Inc.
 Intermountain Oil Marketers Association
 Petroleum Marketers Of Iowa
 Kansas Oil Marketers Association
 Kentucky Petroleum Marketers Association
 Louisiana Oil Marketers Association
 Maine Oil Dealers Association
 Michigan Petroleum Association
 Mid-Atlantic Petroleum Distributors Association, Inc.
 Mississippi Petroleum Marketers Association
 Missouri Oil Jobbers Association
 Montana Chapter, Intermountain Oil Marketers Association
 Nebraska Petroleum Marketers Inc.
 Independent Oilmen's Association of New England
 Fuel Merchants Association of New Jersey
 New Mexico Petroleum Marketers
 Empire State Petroleum Association
 North Carolina Oil Jobbers Association
 Northwest Petroleum Association
 Ohio Petroleum Marketers Association
 Oklahoma Oil Marketers Association
 Oregon Oil Jobbers Association
 Pennsylvania Petroleum Association, Inc.
 South Carolina Oil Jobbers Association
 South Dakota Independent Oilmen's Association
 Tennessee Oil Marketers Association
 Texas Oil Marketers Association
 Virginia Petroleum Jobbers Association
 Washington Oil Marketers Association
 West Virginia Oil Jobbers-Distributors Association
 Oil Jobbers of Wisconsin, Inc.
 Wyoming Petroleum Marketers Association

H. R. 5023

IN THE HOUSE OF REPRESENTATIVES

Mr. SYNAR (for himself, Mr. TAUKE, Mr. WATKINS, Mr. ENGLISH, Mr. RINALDO, Mr. WYDEN, Mr. BEDELL, and Mr. MARKEY) introduced the following bill; which was referred to the Committee on Energy and Commerce

A BILL

1 Be it enacted by the Senate and House of Representa-
2 tives of the United States of America in Congress assembled,

3 SECTION 1. This Act may be cited as the "Petroleum
4 Marketing Practices Act Amendments of 1984".

5 DEFINITIONS

6 SEC. 2. (a) Paragraph (13) of section 101 of the Petro-
7 leum Marketing Practices Act (15 U.S.C. 2801(13)), defining
8 failure, is amended by striking out subparagraph (B) and in-
9 serting in lieu thereof the following:

1 “(B)(i) except as provided in clause (ii), any failure
2 that a franchisor is unable to demonstrate was for a
3 cause within the reasonable control of the franchisee,
4 or

5 “(ii) for purposes of section 102(a)(3), any failure
6 that a franchisor is able to demonstrate was for a
7 cause not within the reasonable control of the franchis-
8 or; or

9 “(C) for purposes of section 102(b)(2)(A) and (B),
10 any failure of the franchisee to purchase or receive on
11 consignment the quantity of motor fuel (by grade or in
12 total) designated by the franchisor, unless the franchis-
13 or can demonstrate that the price and terms (including
14 any special discounts, rebates, or similar allowances)
15 on which the motor fuel was offered to the franchisee,
16 during such period, reasonably enabled the franchisee
17 to compete with comparable motor fuel marketing op-
18 erations operated under a trademark owned or con-
19 trolled by a refiner.”.

20 (b) Section 101 of such Act is amended by redesignating
21 paragraphs (18) and (19) as paragraphs (20) and (21) and by
22 inserting after paragraph (17) the following new paragraphs:

23 “(18) The term ‘constructive termination’ means—

24 “(A) any failure by the franchisor to make availa-
25 ble to the franchisee motor fuel in an amount at least

1 equal to the minimum specified in the franchise agree-
2 ment;

3 "(B) any failure by the franchisor to make availa-
4 ble to its franchisee the amount of motor fuel required
5 by subsection (a) at a price and on terms (including any
6 special discounts, rebates, or similar allowances) which
7 reasonably enabled the franchisee to compete with sim-
8 ilar motor fuel marketing operations operated by, or
9 for, or supplied by the franchisor; or

10 "(C) any downward or upward adjustment to the
11 quantity of motor fuel a franchisee is required or enti-
12 tled to purchase or receive on consignment (by grade
13 or in total) under a franchise agreement or as estab-
14 lished pursuant to any course of dealing unless the
15 franchisor can demonstrate that—

16 "(i) such downward or upward adjustment is
17 applied proportionately to all franchisees, all bulk
18 end-user customers, and all marketing operations
19 of the franchisor operated under a trademark or
20 brand name owned or controlled by the same re-
21 finer which owns or controls the trademark or
22 brand name which the franchisor has authorized
23 the franchisee to use within the relevant geo-
24 graphic market area; or

1 “(ii) if downward adjustment is based upon
2 the failure of the franchisee to purchase or receive
3 on consignment a previously agreed upon amount
4 of motor fuel during a previous period, the
5 franchisor must demonstrate that the price and
6 terms (including any special discounts, rebates, or
7 similar allowances) on which the franchisor was
8 offering to sell or consign motor fuel to the
9 franchisee, during such period, reasonably enabled
10 the franchisee to compete with similar motor fuel
11 marketing operations operated by or for, or sup-
12 plied by, the franchisor within the relevant geo-
13 graphic market area.

14 “(19) The term ‘similar motor fuel marketing oper-
15 ations’, as used in paragraph (18), means the like sale, con-
16 signment, or distribution of motor fuel, other than by the
17 franchisee, under the same refiner-owned or refiner-con-
18 trolled trademark as that which the franchisee is authorized
19 to use.”.

20 CONSTRUCTIVE TERMINATION OF FRANCHISE

21 RELATIONSHIP; TERMINATION AND NONRENEWAL

22 SEC. 3. (a) Subsection (a) of section 102 of the Petro-
23 leum Marketing Practices Act (15 U.S.C. 2802(a)), relating
24 to termination and nonrenewal of franchise relationship, is
25 amended—

1 (1) by striking out "or" at the end of paragraph

2 (1),

3 (2) by striking out the period at the end of para-
4 graph (2) and inserting in lieu thereof "; or", and

5 (3) by adding at the end thereof the following new
6 paragraph:

7 "(3) constructively terminate any franchise rela-
8 tionship."

9 (b) Clause (iii) of section 102(b)(2)(E) of such section is
10 amended by adding at the end thereof the following: "Sub-
11 clause (II) shall not apply unless the franchisor has furnished
12 notification of such sale, transfer, or assignment to the
13 franchisee pursuant to section 104 as if such sale, transfer, or
14 assignment is a termination or nonrenewal, and, during the
15 180-day period after notification has been given, the franchi-
16 sor has made a bona fide offer reasonably related to the value
17 of the premises to sell, transfer, or assign to the franchisee
18 such franchisor's interest in such premises. The requirement
19 in the preceding sentence that an offer be made shall not
20 apply to a franchisor who is a distributor who withdraws
21 completely from marketing motor fuel under a trademark
22 owned or controlled by a refiner in any and all market areas
23 in the United States. Such a distributor who withdraws com-
24 pletely from marketing motor fuel under a trademark owned
25 or controlled by a refiner may at a later time resume sales

1 under a refiner-owned or refiner-controlled trademark if the
2 decision to resume sales under such a trademark is made in
3 good faith and is not intended to circumvent the provisions of
4 this Act.”.

5 (c)(1) Section 102(b)(3)(A) of such Act is amended by
6 adding at the end thereof the following:

7 “(iii) such changes or additions are fair
8 and reasonable.”.

9 (2) Such section is further amended by striking out
10 “and” at the end of clause (i) and by striking out the period
11 at the end of clause (ii) and inserting in lieu thereof “; and”.

12 (d) Subparagraph (A) of section 102(b)(3) of such Act is
13 amended by adding at the end thereof the following: “This
14 subparagraph shall not apply in the case of nonrenewal of a
15 franchise relationship between a refiner franchisor and a
16 franchisee based on the failure of such franchisor and franchi-
17 see to agree to changes or additions to the provisions of the
18 franchise which relate to materially altering, adding to, or
19 replacing the marketing premises which are the subject of the
20 franchise relationship, which shall be governed exclusively by
21 the provisions of subparagraph (D). A change or addition to
22 the terms of a franchise permitting a franchisor, during the
23 term of the franchise, to materially alter, add to, or replace
24 the marketing premises, shall not be implemented until the
25 conclusion of the term of such franchise.”.

1 (e) Subparagraph (D) of section 102(b)(3) of such Act is
2 amended—

3 (1) by striking out “and” at the end of clause (ii),

4 (2) by striking out the period at the end of clause

5 (iii) and inserting in lieu thereof “; and”, and

6 (3) by adding at the end thereof the following new
7 clause:

8 “(iv) with respect to a determination referred
9 to in subclause (IV) of clause (i), a franchisor
10 demonstrates that such determination was neither
11 made with the intent of, nor has the effect of,
12 avoiding competition with the franchisee.”.

13 (f) Paragraph (4) of section 102(c) of such Act is
14 amended—

15 (1) by striking out “and” at the end of subpara-
16 graph (A),

17 (2) by striking out the semicolon at the end of
18 subparagraph (B) and inserting in lieu thereof “, and”,
19 and

20 (3) by adding at the end thereof the following new
21 subparagraph:

22 “(C) in the case of an option to renew or
23 purchase, that such option will not be exercised;”.

24 (g) Subsection (c) of section 102 of such Act is amended
25 by adding at the end thereof the following: “In the case of

1 the failure to exercise an option to renew or purchase, 90
2 days prior to the date of the exercise of such option, the
3 franchisor shall notify the franchisee of such date and of the
4 name, address, and telephone number of the owner or lessor
5 of the underlying lease. If such franchisee enters into an
6 agreement with the owner or lessor to maintain possession of
7 the premises, paragraph (4) shall not be a ground for termi-
8 nation or nonrenewal of the franchise."

9 (h) Section 102 of such Act is amended by adding at the
10 end thereof the following:

11 "(e)(1) Any franchisor who competes with its own
12 franchisees—

13 "(A) for bulk end-user customers,

14 "(B) for other end-user customers to whom motor
15 fuel is sold under a trademark or brand name owned or
16 controlled by the same refiner which owns or controls
17 the trademark or brand name which is the subject of
18 the franchise, or

19 "(C) in the sale of motor fuel for resale under the
20 same refiner-owned or refiner-controlled trademark the
21 franchisee is authorized to use in connection with the
22 sale, consignment, or distribution of motor fuel,

23 must supply motor fuel to such franchisees in a quantity and
24 at a price and on terms (including any special discounts, re-

1 bates or similar allowances) to reasonably enable such
2 franchisee to compete with such franchisor.

3 “(2) For purposes of this subsection, the burden of proof
4 shall be on the franchisor to show lack of competition. Re-
5 strictions imposed by a franchisor on its customers shall not
6 be admissible to show lack of competition between a franchi-
7 sor and franchisees. With respect to commercial or consumer
8 accounts and refiner supplied franchisee retailers located in
9 the same relevant geographic market area, a distributor who
10 is a franchisee and a refiner who is that distributor’s franchi-
11 sor shall be presumed to be competitors.”.

12 TRIAL FRANCHISES

13 SEC. 4. Paragraph (2) of section 103(b) of such Act (15
14 U.S.C. 2803(b)), relating to trial franchises, is amended to
15 read as follows:

16 “(2) The term ‘trial franchise’ does not include—
17 “(A) any unexpired period of any term or
18 any franchise (other than a trial franchise, as de-
19 fined by paragraph (1))’ which was transferred or
20 assigned by a franchisee to the extent authorized
21 by the provisions of the franchise or any applica-
22 ble provision of this Act or State law which per-
23 mits such transfer or assignment, without regard
24 to any provision of the franchise, or

1 “(B) any subsequent franchise with the
2 transferee or assignee.”.

3 ENFORCEMENT

4 SEC. 5. (a)(1) Section 105 of the Petroleum Marketing
5 Practices Act (15 U.S.C. 2805(d)) is amended by redesi-
6 gnating subsections (b) through (e) as subsections (c) through
7 (f), respectively, and by inserting after subsection (a) the fol-
8 lowing new subsection:

9 “(b) If a franchisor constructively terminates a fran-
10 chise, the franchisee may maintain a civil action against such
11 franchisor as set forth in subsection (a).”.

12 (2) Such section is amended in subsection (f)(2), as re-
13 designated by paragraph (1), by striking out “(d)” and insert-
14 ing in lieu thereof “(e)”.

15 (3) Subsection (e) of section 105 of such Act, as redesign-
16 nated by paragraph (1), is amended by striking out “prevails
17 in any action under subsection (a)” and inserting in lieu
18 thereof “prevails in any action under subsection (a) or is
19 granted equitable relief under subsection (b)”.

20 (4) Subparagraph (A) of section 105(e)(1) of such Act, as
21 redesignated by paragraph (1), is amended by adding before
22 the semicolon the following: “or final equitable relief”.

23 (5) Subparagraph (B) of section 105(e)(1) of such Act, as
24 redesignated by paragraph (1), is amended by inserting after

1 "thereunder," the following: "or in the case of a willful con-
2 structive termination of the franchise,".

3 (6) Paragraph (3) of section 105(e) of such Act, as re-
4 designated by paragraph (1), is amended by inserting after
5 "subsection (a)" the following: "or subsection (c)".

6 SALES, TRANSFERS, AND SUCCESSION

7 SEC. 6. (a) Title I of the Petroleum Marketing Practices
8 Act (relating to franchise protection) is amended by adding at
9 the end thereof the following:

10 "SALES, TRANSFERS, AND SUCCESSION

11 "SEC. 107. (a) If, prior to the death of the franchisee,
12 retirement of the franchisee, or continuing severe disability of
13 the franchisee as set forth in section 102(c)(4), the franchisee
14 provides the franchisor a succession plan to provide for dispo-
15 sition of the franchise relationship upon such death, retire-
16 ment, or disability, such death, retirement, or disability shall
17 not be grounds for termination or nonrenewal of the franchise
18 relationship.

19 "(b) Subsection (a) shall not apply if—

20 "(1) the franchisor notifies the franchisee in writ-
21 ing, within 30 days after receipt of the succession plan,
22 that the franchisor rejects such plan.

23 "(2) such rejection notice includes the reasons for
24 such rejection, and

25 "(3) such rejection is reasonable.

"Sec. 107. Sales, transfers, and succession."

EFFECTIVE DATE

16 SEC. 7. The amendments made by this Act shall take
17 effect on the date of the enactment of this Act.

Senator MATHIAS. Mr. Columbus.

STATEMENT OF R. TIMOTHY COLUMBUS

Mr. COLUMBUS. Mr. Chairman, my name is Tim Columbus. I am a member of the law firm of Collier, Shannon, Rill, and Scott, and I am appearing today on behalf of our client, the Society of Independent Gasoline Marketers of America.

SIGMA is a trade association comprised of approximately 250 independent marketers and chain retailers of motor gasoline, who operate in 49 of the 50 States. The association members' sales represent between 10 and 15 percent of the domestic retail market for motor gasoline.

The Association's members also range in size from firms which operate as few as two retail outlets to firms which operate several hundred retail outlets.

Marketers, such as SIGMA's members, historically have been the most innovative and cost-effective segment of the gasoline marketing industry. Such marketers pioneered the high volume/low margin marketing concept, as well as self-service. They consistently have been the most consumer-sensitive portion of the retail market and historically have delivered gasoline to motorists at the lowest possible price by minimizing the amount of fixed operating costs which must be recovered in their per-unit selling price of gasoline.

At the outset, I think it is important to recognize what a SIGMA member does for a living. He acquires refined petroleum products from a supplier, and he sells those products to consumers. Thus, he is effectively in the same business as a retail dealer. His superior efficiencies in performing his marketing functions supply him with whatever competitive advantages he enjoys. However, to make his efficiencies relevant in the market, he must be able to acquire products at a cost which is roughly equivalent to the costs incurred by his competitors.

Historically, traditional market forces, that is, competition, have assured such a marketer that he could fulfill this condition precedent to his economic and competitive viability.

Recently, many marketers have had difficulty obtaining product on this basis, and this situation has caused substantial concern to SIGMA. Because of marketers' dependence on the operation of competition at the wholesale level, they are, as well as everybody else, vulnerable to predation by integrated companies. Given these economic realities, SIGMA has a keen awareness of and sensitivity to circumstances which threaten effective competition and as a result, the viability of its members.

SIGMA strongly supports this committee's willingness to address the critical issue of the structure of the petroleum industry in general and the motor fuels market in particular. S. 40 clearly reflects its sponsors' recognition that something is radically wrong in the industry.

We believe that if recent dislocations and disparities are not recognized and remedied immediately, the long-term prospects for the competitive viability of independent marketers, and therefore consumers, who have been able to historically rely on this segment for protection from unnecessarily high prices, are bleak. However,

SIGMA does not believe that the proposed legislative prohibition on participation in the market by certain competitors or the proposed alteration of contractual obligations which are proposed in S. 40 constitute an adequate or appropriate response to problems reflected in today's market.

Rather, SIGMA believes that the consumer, as well as participants in the motor fuels market, would be better-served by Congress' closely addressing the trend towards increased concentration in the market and the administration of the antitrust laws in the context of the petroleum industry.

Mr. Chairman, SIGMA basically opposes two operative provisions of S. 40. With respect to the divorcement provisions, I think a few points are relevant.

First and foremost, SIGMA does not perceive divorcement as the solution to the real problem in the marketplace, which is the apparent ability of some competitors to render irrelevant the functional efficiencies of other competitors in the market. Specifically, over the past couple of years, a number of refiners have demonstrated an ability to increase dramatically their market share through dealer organizations by controlling dealers' resale prices through rebates, discounts, zone-pricing, and a good program of enforcement of that kind of exercise.

In short, divorcement at best addresses only one symptom of what may be a bigger disease. Moreover, we fear that the focus of legislative attention on the concept of divorcement diverts attention from a much more basic problem.

Finally, SIGMA really looks at itself and its members as the ultimate target of this legislation. We have watched this evolve in the States, where refiners, big refiners are the first target, then all refiners, then we move on to jobbers and ultimately to chain retailers.

I have run out of time, and Senator, I would be happy to respond to any questions the committee might have. We really feel this is the wrong answer to the wrong problem, and we would urge you to take a look at things in a much broader scope.

Thank you.

Senator MATHIAS. Thank you very much.

[The following was received for the record:]

Testimony of
R. Timothy Columbus
on behalf of the
Society of Independent Gasoline Marketers of America

My name is R. Timothy Columbus. I am a member of the firm of Collier, Shannon, Rill & Scott and am appearing today on behalf of our client, the Society of Independent Gasoline Marketers of America ("SIGMA"). SIGMA is a trade association comprised of approximately 250 independent marketers and chain retailers of motor gasoline. SIGMA members market gasoline in 49 of the 50 states through approximately 13,000 retail outlets. SIGMA members' sales represent between 10 and 15 percent of the domestic retail market for motor gasoline. SIGMA members range in size from firms which operate two retail outlets to firms which operate several hundred retail outlets.

Marketers, such as SIGMA's members, historically have been the most innovative and cost-effective segment of the gasoline marketing industry. Such marketers pioneered the high volume/low margin marketing concept. They consistently have been the most consumer sensitive portion of the retail market and historically have delivered gasoline to motorists at the lowest possible price by minimizing the amount of fixed operating costs which must be recovered in their per unit selling prices. Simply stated, independent marketers and chain retailers built their businesses on the basis of their marketing efficiencies and are the most efficient retailers of gasoline in the domestic market. As such, they historically have been the price-conscious gasoline consumer's best friend. However, as marketing, rather than manufacturing, companies, SIGMA members are able to fulfill their historic market role only under conditions in which they can obtain adequate supplies of gasoline at a cost which permits them through their marketing efficiencies to compete effectively in the retail market.

At the outset, one must recognize what a SIGMA member does for a living. He acquires refined products from a supplier and sells them to consumers. His superior efficiencies in performing his marketing functions supply him with the competitive advantages he

enjoys. To make his efficiencies relevant in the market he must be able to acquire products at a cost which is roughly equivalent to the cost incurred by his competitors. Historically, traditional market forces, i.e., competition, assured such a marketer that he could fulfill this condition precedent to his economic and competitive viability. Recently, many marketers have had difficulty obtaining product on this basis and this situation has caused substantial concern to SIGMA. Given these economic realities, SIGMA has a keen awareness of, and sensitivity to, circumstances which threaten effective competition and as a result the viability of its members.

In sum, SIGMA members are retailers of motor fuels. They are in the same business as "dealers." As such, they are extraordinarily vulnerable to predatory practices by their more powerful, fully integrated competitors. Moreover, because they historically have been at the cutting edge of competition and marketing innovation, their disappearance from the marketplace would be a tragedy for consumers.

SIGMA strongly supports this Committee's willingness to address the critical issue of the structure of the petroleum industry in general and the motor fuels market in particular. S.40 clearly reflects its sponsors' recognition that something is radically wrong in the industry. We believe that if recent dislocations and disparities are not recognized and remedied immediately the long-term prospects for the competitive viability of independent marketers, and therefore for consumers who have been able historically to rely on this segment for protection from unnecessarily high prices, are bleak. However, SIGMA does not believe that the proposed legislative prohibition on participation in the market by certain competitors or the proposed alteration of contractual obligations contained in S.40 constitute an adequate or appropriate response to the problems reflected in today's market. Rather, SIGMA believes that the consumer, as well as participants in the motor fuels market, would be better served by Congress' closely addressing the trend towards increased concentration in the market and the administration of the antitrust laws in the context of the industry.

SIGMA's Concerns Regarding
the Provisions of S.40

S.40 contains two proposed prohibitions to which SIGMA objects: (1) the prohibition against certain refiners' operation of any motor fuel service station in the United States (the divorcement provisions); and (2) the prohibition against enforcement of exclusive supply arrangements between a dealer and a refiner or distributor (open supply). SIGMA opposes these proposed prohibitions on both philosophical and practical grounds.

SIGMA's opposition to the divorcement provisions of S.40 reflects the Association's concern that these provisions, if enacted, could serve as a precedent for further legislative apportionment of the retail market. Moreover, SIGMA sincerely doubts that the Federal Government's intervention in the retail market for motor fuels in the manner envisioned by S.40 would contribute substantially to the alleviation of the problems existing in that market.

SIGMA perceives the divorcement provisions of S.40 as an attempt to avoid integrated refiners' gaining control of the retail market through predatory practices. SIGMA doubts that legislatively limiting the right of certain companies to operate retail outlets would effectively prohibit integrated companies' achieving domination of the retail market if that is, in fact, their intention.

During the last two years, integrated companies have demonstrated their ability to garner substantial market share, and the market power attendant to it, through means other than directly operated retail outlets. Specifically, by employing a well-coordinated program of rebates and discounts, tied to zone pricing schemes, major integrated companies can increase their share of the retail market substantially. Information submitted to SIGMA suggests that the pricing programs of particular companies, when coupled with an effective program of control over the resale price of those companies' dealers, has resulted in substantial gains in controlled market share without the burden of direct operation of retail outlets. Thus, if the objective of the divorcement provisions of S.40 is to limit the share of the retail market over which integrated companies exercise control, then SIGMA considers these provisions an ineffective means by which to obtain this objective.

SIGMA is concerned that the focusing of legislative efforts on the enactment of a potentially ineffective remedy will have the undesired result of distracting Congress' attention from problems of a much more substantial nature. Moreover, the enactment of the divorcement provisions could serve as a highly undesirable precedent for future efforts to apportion legislatively the retail market of which distributors and chain retailers would be the target.

In summary, SIGMA opposes the divorcement provisions of S.40 because the Association believes that they do not constitute an effective solution to the problems in the retail market for motor fuels and because the Association fears that its members would be a target for similar legislation in the future. SIGMA requests that this Committee instead focus its attention on those circumstances which threaten the relevance of functional efficiency in the retail market and thereby the essence of true competition. Simply stated, retail marketing divorcement addresses only one apparent symptom of a problem, it does not address that problem's the root causes.

SIGMA's objection to the "open supply" provisions of S.40 are less broad in nature. SIGMA does not view this provision as "structural." Rather the question raised by these provisions is one of fundamental fairness.

Exclusive supply arrangements frequently reflect a distributor's or a refiner's strategy not only for the disposition of its fuel, but also for obtaining a return on its real estate investment. It is essential that the Committee recognize that a legislative prohibition on the absolute enforcement of exclusive supply agreements may result in a substantial injury to the lessee-dealers who apparently are a part of the class intended to benefit from these provisions. This injury would arise when a supplier is faced with the reality that the only means by which to obtain an adequate return on its real estate investment is to provide for such a recovery in the form of rent.

Frequently a supplier-lessor obtains a portion of its return on real estate investments in the form of the price it charges for motor gasoline supplied under an exclusive supply agreement. If such a supplier-lessor is no longer guaranteed the customer loyalty for which it contracted, then it is logical that that supplier-lessor will

be required to make alternate arrangements to achieve its return on investment. Such alternate arrangements can only constitute an increase in rental charges.

A second concern with respect to the open supply provisions is one of fundamental fairness to branded suppliers as well as to customers. Specifically, branded dealers are afforded the benefit of advertising campaigns and other services associated with the brand name. Customers frequently are attracted to an outlet by these services. It appears essentially inequitable to deprive the branded supplier of the benefit of its bargain by permitting a branded dealer to market unbranded fuels, even if such unbranded fuels are clearly identified as such. This question of equity is particularly concerning when one realizes that the contractual terms which the open supply provisions would effectively abrogate are the result of negotiations between the parties.

Recommendations

SIGMA recommends that S.40 not be enacted. Rather, SIGMA believes that the Committee should focus its efforts on addressing those circumstances which, to an increasing extent, are rendering the functional efficiencies of particular participants in the retail market totally irrelevant to their long-term economic viability. Specifically, it has been the common wisdom in this industry over the years that an entity which can perform a particular function in the marketplace at a smaller cost than its competitors will survive and ultimately prosper. Calls for divorce legislation essentially reflect the view by some that integrated companies' operation of retail outlets is undertaken on a basis which renders its competitors' functional efficiencies irrelevant. However, if integrated companies are undertaking predatory practices in an attempt to dominate the retail market, their direct operation of retail outlets on a non-economic basis is only one symptom of a more serious disease.

SIGMA urges the Committee not to abandon its efforts to ensure that consumers receive the benefit of intense, healthy competition. Rather SIGMA urges the Committee to focus those efforts on the circumstances which encourage the predatory practices which threaten the structure of competition at the retail level. A

refocusing of the Committee's attention on fundamental circumstances, such as the alarming trend towards concentration of control over crude oil and other natural resources resulting from the recent wave of mergers in this industry. The Committee's scrutiny of such mergers and its insistence that any such mergers not result in effective reduction of competition would be a more productive step than pursuing S.40.

SIGMA appreciates this opportunity to share its views with the Committee. I will be happy to respond to any questions which my testimony may have raised.

Senator MATHIAS. Senator Metzenbaum, who is detained, has sent me a message and asked me to put one question to Professor Umbeck. That is, he would like to know whether you are here pro bono, or whether you are here in a representative capacity.

Mr. UMBECK. I was invited to speak by Atlantic Richfield Co. They are paying my expenses.

Senator MATHIAS. Thank you very much.

Now, we will review the statements as in the case of the first panel, and will probably have some written questions, on both my behalf and in behalf of other members of the committee.

But let me put to you the same question I put to the first panel, as to why you see the inching up of prices. I was glad to hear that in the Louisiana area, they are exempt from that problem, but in many other parts of the country, oil prices and gasoline prices do seem to be inching up.

Yes?

Mr. REILLY. Mr. Chairman, I must admit I am a little amused, only because we are addressing why prices are going up here. I have two appointments today with Members of Congress, and I have to explain why our prices are so low. I guess it proves you have to be flexible in today's world.

Senator MATHIAS. I am only reacting to what I see when I go into my neighborhood gas station.

Mr. REILLY. Yes, that is usually when the consumer does react.

Mr. NICHOLSON. And do you live in Maryland, sir?

Senator MATHIAS. I do. [Laughter.]

Mr. REILLY. I think gasoline is just like any other commodity in our country, and the price of it reacts, obviously, to the costs involved in producing it and to the swings in demand, so simple old supply and demand.

I obviously cannot speak for the industry, but I will speak for the Atlantic Richfield Co. In the Western part of the country, where our prices over the last couple of months have been the lowest that they have been in sometime, the market has gone up. And in response to that, we have raised our prices in the West.

On the east coast, however, including the State of Maryland, Pennsylvania, and this area, prices have been relatively low and

relatively stable, and we have not had any significant price movement upward in several weeks now.

I am glad to hear you say that. I hope the prices do edge up a little bit. We could use it.

Senator MATHIAS. Well, how widespread is it? Mr. Nicholson implies this is just a Maryland phenomenon.

Mr. NICHOLSON. Well, Senator, it is my belief that the gasoline market is a highly competitive market. Mr. Chisholm also spoke about that. And each individual market responds differently to the pressures within that market, and I think you could go across this country and look at all the markets, and you could see price trends upward or downward. The price changes daily on the spot market, and it is a reaction to those changing competitive conditions; they are changing the prices both ways all over the country.

Senator MATHIAS. Well, it is not just a Maryland phenomenon. My grandmother was born on a farm in the Shenendoah Valley, right on the Virginia-West Virginia border, and that is where I am a real gasoline customer, not my 1977 Vega; that does not burn very much gas, but my tractor does. And I find that in a non-Maryland market, I have a rising gasoline bill as well as in the Maryland market.

Mr. NICHOLSON. Well, my observation would be that prices are going both ways in the areas in which we market, Senator. I think it is just a visible sign of the competition in the gasoline market.

Senator MATHIAS. Well, I can understand that you and I may have varying reactions, as sellers and buyers, but I hope that I get into one of those swings where I can enjoy the down side.

I am told that the very distinguished Senator from Delaware, Mr. Biden, is coming, and that he has some questions that he would very much like to put to this panel. As I said at the outset, I am anticipating the sergeant-at-arms with a wrecker to haul me away, and before he gets here, I am going to have to leave. So what I will do is put the committee into a brief recess pending the arrival of Senator Biden. If he does not get here by 10:30, we will stand adjourned subject to the call of the Chair.

So the committee stands in recess until Senator Biden's arrival.
[Short recess.]

STATEMENT OF SENATOR JOSEPH R. BIDEN, JR.

Senator BIDEN. The hearing will reconvene.

I would like to thank the panel and thank Senator Mathias for waiting. I was at another committee meeting, and I understand your testimony has already been given. I am not going to keep you long, and I may very well repeat some of the questions you have already been asked—if I do, please tell me they have already been asked, and I will read the record. But there are a few things I would like to pursue, and I will not keep you more than 10 or 15 minutes, if I may.

One of them is something that you may not have expected—and this is to the entire panel, but particularly to Mr. Columbus of the Society of Independent Gasoline Marketers of America—as you all know, there is a mild bit of activity relating to mergers these days. There seems to be something in the air. And there is something in

the air down here in Washington about dealing with mergers. Now, I realize that is not the subject matter of the service station legislation, but I think it may have an impact. I am wondering whether or not this bill will have an impact if the merger activities continuing; and, of course, assuming that there is no legislation along the lines proposed by Senator Johnston or anyone else, that would impact upon the ability of the majors to merge, the major oil companies, and the merger fever continues.

IMPACT OF MERGERS

I will begin with you, Mr. Columbus, if I may. What impact will such mergers have upon the independent gasoline dealers. Where is their fate? Where do they end up?

Mr. COLUMBUS. It is the concern of the association which I represent that a continued trend toward increased concentration in the industry bodes very poorly for the chain retailer, particularly private brand operation. Specifically, the functional efficiencies of those operations in delivering gasoline to the consumer are dependent upon the companies who perform those services being able to buy gasoline at a competitive price at the wholesale level. What we are watching with this wave of mergers is the disappearance of potential sources of supply—and I will use the Texaco-Getty proposed consent decree as an example—the substitution for a viable supplier of something that at least theoretically may look good, but in the context of today's market, really does not look good at all. The example I would like to refer to, Senator, is the proposed spin-off of the refining facilities in Eldorado, KS. That refinery historically has been very much of a balance wheel in the supply of product in that part of the world. First of all, not only does Getty supply the unbranded marketers directly, but it also serves as an exchange point for other major suppliers to put product into that market. It is the Association's concern that if that refinery is simply spun off without the necessary crude oil reserves to back it up, it will no longer be able to perform that function. If you look at Socal/Gulf, we do not know what, if any, divestiture would take place after that acquisition.

I think the key point is that we will only survive to the extent there is vital and strong competition at the wholesale level. Independent refiners over the last couple of years have had an increasing amount of difficulty performing that function, and we are very concerned about the disappearance of potentially strong and historically viable competitors from the marketplace.

Senator BIDEN. Yes, sir?

Mr. CHISHOLM. Senator Biden, I am Phil Chisholm, the executive vice president of the National Oil Jobbers Council. By and large, I would like to echo what Mr. Columbus said.

Our membership views the recent rash of mergers as being perhaps the most serious issue facing our membership today.

There is a huge degree of concern over many of the matters that Mr. Columbus raised, not only from the standpoint of what it means for private brand marketers, but what it means for branded marketers in many of those areas, because you have marketers who have operated under the Getty brand for years and years and

years. You have a truckstop chain throughout the Midwest that has been operated under the Getty brand for years and years and years. And there is virtually no outlook for who is going to take that over at this point.

As Tim pointed out, there is no crude agreement going into that Eldorado refinery, and even if there were a supply agreement, there is a question of what price crude would be supplied at to whomever purchases that refinery.

And unless the Government, as FTC appears to be willing to do to regulate crude oil prices, as they have proposed to do on the west coast, in the instance of forcing Texaco to supply crude oil there, we are just not sure how that is going to work.

That is just one example, but those are the types of concerns we certainly have with the Gulf/Socal merger, and we would certainly urge whatever action the House and the Senate can take in forwarding legislation which would at least put on hold for a little while these mergers until they can be more closely examined.

Senator BIDEN. Mr. Nicholson?

Mr. NICHOLSON. Well, Senator, I think you have to look at the overall petroleum market for a moment. It is a worldwide market. There are products in crude oil around the world that can be imported into the United States, and so you have to look at it on that basis. It is highly competitive. Most refineries are not full, and therefore there would be capacity.

Marathon is one of the largest suppliers to the independent segment of the market, represented by the two gentlemen on my right. Our refineries are not full. We have a similar situation, in a way, in those markets, and of course, some marketers have withdrawn. Marathon views those as opportunities, and I believe that the market demands will be met in a highly competitive manner if there is no legislation, as has been suggested by—

Senator BIDEN. With all due respect, Mr. Nicholson, what does that mean? You sound like you are from the State Department. Tell me what happens to "Charlie Schmedlap," who runs the gas station in Delaware that has a big "Getty" sign on it right now, and now there is a merger, and what happens now is Texaco ends up picking up that piece of it. What happens to "Charlie Schmedlap?"

Mr. NICHOLSON. Well, I think in a way, it would be what happened to a fellow who had an Arco station in Ohio. When Arco left, Marathon took those over. He now has a Marathon brand on his station, and we think he is happy to be associated with us.

It is a highly competitive market where people are fighting for market share. I think there will be other suppliers willing to supply those people.

Senator BIDEN. Yes, sir?

Mr. REILLY. Senator, I am Ed Reilly from Atlantic-Richfield. I generally agree with that. In answer to your question of what is going to happen to that individual dealer, I do not think anybody knows. He might very well end up better off than he is today; it is conceivable that he might not.

As Mr. Nicholson said, we spun off Ohio for economic reasons, and they picked them up. We have had mergers in the past with both Sinclair and Richfield on the west coast, and have melded the

three companies together into what I think is generally recognized as a fairly successful-type merger.

The refinery that was referred to, whether there is a merger or is not a merger, it is going to pretty much exist or not exist based on the economic merits of the operation of that refinery or any refinery.

Senator BIDEN. While I have you all here, what do you think about this legislation—the legislation to slow up, stop, delay, postpone mergers?

What do you think about so-called “golden parachutes” and things like that. I would like to know what you think about, first of all, the legislation relating to the attempt to block mergers.

Mr. COLUMBUS. Senator, the Society of Independent Gasoline Marketers of America support that legislation.

Mr. CHISHOLM. Senator, the National Oil Jobbers Council will support it, as well.

Mr. REILLY. I think you have to ask yourself why—why do you need that legislation. And if there are compelling reasons that are obvious and not emotional, to have that type of legislation, then perhaps it is something that should be looked at. But I think it is important to have reasons as to why that type of legislation is required, and not just because something is happening in the marketplace, whether it be the petroleum industry or any other industry, to just suddenly rush, hellbent for new legislation.

Mr. UMBECK. Senator, if I may, I am John Umbeck, an economist from Purdue University. Backing up to your first question and relating also to your second one, the evidence right now, at least among economists, is that there is absolutely no indication that mergers of this type will have any significant effect on average on your market. Some people are going to be better off, some are going to be worse off. But in terms of average retail prices, volumes, throughputs, all of the things that concern us as consumers, there is no indication that mergers of this type will have any effect.

Now, I do have to qualify that. That assumes that these mergers will take place in an environment in which there is legally-allowed entry—that is, as government regulations are put into place which restrict entry, which will limit incoming competition, mergers of this type can have some consequences not necessarily favorable to the consumer.

Senator BIDEN. As a practical matter, do such mergers have that impact?

Mr. UMBECK. Again, in the environment that we have right now, I anticipate very trivial effects of mergers of this type—.

Senator BIDEN. In terms of new entries.

Mr. UMBECK. I do not think it will have any impact at all on new entry.

Senator BIDEN. Why? I have not taken a position on the bill. I am anxious to know why.

Mr. UMBECK. Because there is no indication that these mergers are going to make it to alter the gains or the costs to an incumbent potential competitor. If he wants to come in, he will still have access to exactly the same resources that he had prior to the merger. The merger is not taking any additional resources out of

play. It is merely combining ownership of an existing set of resources.

Now, my qualification was aimed in part at the bill we are talking about today; divorcement legislation and bills of this type, which restrict entry of certain types of organizations, of certain types of contract structures, which are designed to market or wholesale or produce or refine crude, can exacerbate the effects of these types of mergers.

Senator BIDEN. In what way would that happen?

Mr. UMBECK. Pardon?

Senator BIDEN. In what way could they do that?

Mr. UMBECK. Well, a merger to the extent that it concentrates ownership and occurs in an environment in which there is limited access will now give the larger companies greater control over the existing resources, and by not allowing new people to come in and compete with them, will give them increased market power.

But to the extent that you allow small refiners to come in and salary-operated stations, to the extent that you do not prohibit this, any effects of the merger will be immediately gobbled up by new competition, coming in and taking advantage of any possible increased price that might emerge from these situations.

Mr. COLUMBUS. Senator, if I may, the gentleman from Arco suggested that we ought to have some reasons to support that legislation, and I will at least tell you what my client's considerations are. One, it is based to a large extent on uncertainty. With Texaco-Getty, and now the proposed merger of Socal and Gulf, my clients view this as a substantial potential for restructuring the wholesale and retail markets for product. And that is something that should not be undertaken lightly and without some sort of understanding of what the implications of it are.

They are also concerned about the potential implications for the concentration and control over crude oil and what effect that has with respect to the crude oil market for independent refiners who serve as sources of supply.

In addition, I think they are concerned about what does it mean, just in terms of national energy policy on the whole. Remember, this is not just the oil and gas business that these companies are merging. You have got coal, you have got a lot of things. And until Congress has had an opportunity to take a look at that and really understand the potential implications of it, we think somebody ought to put the brakes on.

Mr. CHISHOLM. I think in addition to those, one of the other reasons we are supporting it is that—well, I should preface that by saying that NOJC did not take a position per se on the Texaco-Getty merger, but after seeing the FTC consent order, all sorts of alarms went off and raised all sorts of concerns. Then we see Gulf-Socal; you have Mobil-Superior; you have rumors throughout the industry of who is next to be taken over, with several companies being mentioned prominently. You have people sitting on lines of credit, that they can go out and purchase these companies. And the mentality which seems to be prevailing in the industry, that the best way to prevent yourself from being taken over is to go out and leverage yourself so badly that no one would want to take you over, is a great concern to our membership. I mean, you can argue that

maybe Texaco-Getty in isolation, or even Gulf-Chevron in isolation, may be justifiable. But when you put these various pieces of the puzzle together and see the picture that begins to emerge, it is scarey as hell.

Senator BIDEN. Would anyone else like to comment?

Mr. UMBECK. At the present time, we are undertaking research in which we explore the effect of concentration by a particularly brand in local markets, which is one of the issues underlying this whole merger situation. That is, in markets where you have a high percent of one brand name, where a major occupies, let us say, 30 to 50 percent of the developed retail sites, how does this impact on retail prices, credit, hours, and other services?

To date, we have found absolutely no significant effects of any kind. Again, it just substantiates what I was saying, that in a market where you do have relatively easy access to entry by newcomers, there is absolutely no reason to expect these concentration ratios to have any impact at all on retail performance.

Senator BIDEN. I have no further questions.

Thank you very much, gentlemen.

Mr. Rasheed, if you would like to come up and sit down. The rest of you gentlemen are excused. Just another minute or two, Mr. Rasheed. Have a seat. I am not going to call back the rest of the panels, though.

Mr. RASHEED. Thank you, Senator Biden.

I represent the Service Station Dealers of America. My name is Vic Rasheed. I am the executive director.

I think if you look at my testimony which I gave earlier, I devoted a great deal of it to detailing what is happening in the Canadian market. There, they have a situation which is rapidly, or could develop in this country, and that is the reason that I referred to it. They have six refiners who will soon be five; they have total control, not just of wholesaling and refining, but they also now have almost total control of setting the retail prices that the once independent service station dealers, who are now all reduced to commission agents because they could not compete with the suppliers. They have almost a monopoly of the Canadian market.

The Canadian Government has spent a great deal of time investigating ways to try to restore competition. They traced the monopoly to the point where the five major American companies that operate are now being accused of charging a higher price for crude oil to their Canadian subsidiaries in Canada, so that the price of gasoline charged to Canadians is higher than it should be. In effect, what they are looking at is a monopoly situation which has developed in Canada, which has been allowed to develop, because five major refiners have effectively taken over the market from refining, distribution, and now retailing. I think that is what we are faced with in this country, and I think S. 40 is very relevant, because this is the first step to really stopping that type of situation developing. I think we have to take steps to do that now.

So certainly, we oppose these mergers. I think they are not in the best interest of the consumer any way you look at it. And the bottom line will be the price that consumers will have to pay for gasoline in the future.

Senator BIDEN. Thank you.

I want to make it clear—I indicated I had not taken a position on the issue. The issue I was referring to was the merger legislation, not this legislation.

Mr. RASHEED. I understand, but I do think the two are related.

Senator BIDEN. Yes, and I will read your testimony.

Mr. RASHEED. Thank you.

Senator BIDEN. Thank you very much.

The hearing is closed.

[Whereupon, at 10:42 a.m., the committee was adjourned.]

[The following letter and statement was subsequently supplied for the record:]

APPENDIX



THE STANDARD OIL COMPANY

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TELEPHONE 402-765 4566

WILLIAM C. ROUNTREE
DIRECTOR
FEDERAL GOVERNMENT AFFAIRS

April 13, 1984

Honorable Strom Thurmond
Chairman, Senate Committee on
the Judiciary
SD-224 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Mr. Chairman:

Please include the enclosed statement of the Standard Oil Company (Ohio) in the record of the March 14 hearing held by the Senate Judiciary Committee on S.40, the Small Business Motor Fuel Marketer Preservation Act. SOHIO is strongly opposed to this legislation that appears to be designed to remove a legitimate competitive force from the marketplace at a significant cost to the consumer.

Thank you for allowing our statement to appear as part of the hearing record.

Sincerely,

William C. Rountree

enclosure
cc: Members, Senate Judiciary Committee

STATEMENT OF
THE STANDARD OIL COMPANY (OHIO)
TO THE
SENATE JUDICIARY COMMITTEE
REGARDING S. 40
MARCH 14, 1984

HUGH D. HANNA
VICE PRESIDENT, RETAIL MARKETING
THE STANDARD OIL COMPANY (OHIO)

This is a statement of The Standard Oil Company (Ohio) submitted by Hugh D. Hanna, Vice President, Retail Marketing, regarding S. 40, entitled "Small Business Motor Fuel Marketer Preservation Act". Essentially, S. 40 contains the same key provisions as S. 326 and S. 2798 on which hearings were held during 1980 and 1981. The Standard Oil Company (Ohio) submitted testimony for the record at those hearings. This statement draws from the prior testimony and also presents new material in opposition to S. 40.

As introduced, S. 40 would prohibit all major refiners from operating retail gasoline outlets with company personnel. The bill, however, would place no restrictions on "small" and "independent" refiners regarding operation of company outlets. Further, it would permit "open supply" with multiple branding at service stations under certain circumstances.

The Standard Oil Company (Ohio) is opposed to S. 40. It is anti-consumer, special interest legislation designed to remove a legitimate competitive force from the marketplace at a significant cost to the consumer.

S. 40 has been introduced in response to organized dealer allegations that the decline in the number of retail service stations and the reduction in the proportion of gasoline volume moved through dealer outlets since 1972 has been the direct result of a concerted effort by refiners to eliminate dealers. They contend that refiners have engaged in predatory pricing and have subsidized company-operated stations with profits from other operations.

It is our contention that the dealers' allegations do not stand up to the facts of the marketplace. Petroleum marketing has been undergoing a metamorphosis of facilities. It is this same type of restructuring that took place in food distribution 50 years ago with the introduction of the supermarket. The significant decline in the number of service stations has been caused by rapidly changing buying patterns as well as basic service station economics.

Following World War II, the service station population increased markedly as the automobile population and gasoline sales expanded. Americans moved away from the center cities of major metropolitan areas into suburban communities and also engaged in extensive long distance travel via the newly-constructed interstate highway system. New service station construction followed the consumer migration and took the form of conventional two and three-bay facilities which could provide gasoline and minor automobile maintenance work at the same location.

By the mid-1970s the rapid growth in the service station population of the '50s and '60s was looked back upon as "overbuilding". Consumer buying patterns for gasoline and automotive products were changing rapidly and gasoline prices had jumped precipitously following the Arab oil embargo, slowing the growth in demand. In fact, this was the beginning of a change in American life style that included the shift from large, high consumption automobiles to more modest, fuel efficient vehicles. Since the peak in 1978, U.S. gasoline demand has dropped by 13% and demand in Ohio, our prime market, has declined by 18%.

While there had been great similarities in the marketing strategies of the various competitors up to the late 1960s, the introduction of gasoline-only facilities by efficient, low-priced private brand marketers signaled the beginning of market segmentation. This was followed by the sale of gasoline at car washes and convenience food stores and the introduction of self-serve gasoline stations.

A growing number of customers have responded to the appeal of these marketing innovations. The growth of convenience stores and the sale of gasoline at these facilities is a logical evolution from the changing way of life in American homes. Whereas only 10% of women with children under six years of age were working in 1950, by 1982 this percentage had increased fivefold to 50%. Working women need convenient places to "fill in" on grocery needs and the purchase of gasoline along with the food items saves them very precious time.

In auto services, young motorists who are changing their own motor oil, tuning the engines of their cars, and making other automotive repairs, are no longer willing to pay the higher gasoline prices associated with full-facility outlets. Today, the "do-it-yourself" market accounts for over two-thirds of antifreeze sales, half of the oil changes, and nearly 40% of the tune-ups and brake jobs performed.

Similarly, technological changes have been taking place in automobiles as Detroit has responded to consumers' desires for more maintenance-free automobiles. The

changes have been gradual but very dramatic when looked at over time. For example, the oil change interval has increased from every 2,000 miles in the mid-'50s to every 7,500 miles today. Instead of a tune-up every six months or 5-6,000 miles, one every two years or 20-25,000 miles is now prescribed. Bias tires which ran 15-18,000 miles have been replaced by radials which commonly run 40,000 miles.

Finally, the implementation of new technology has resulted in far greater sophistication in recent automobile models than in those of only a few years ago. This, in turn, has created a demand for a higher level of proficiency in auto maintenance than available at many service stations.

All of these changes have had a radical impact on "traditional" service stations. Consumers in increasing numbers have deserted these outlets and have moved significant gasoline volume to price-oriented, gasoline-only outlets, convenient stores, and car washes. Likewise, they have moved auto service to specialized units. Thus, conventional facilities have declined in numbers and in overall marketing strength, regardless of how they have been operated -- by dealers, by employees of major oil companies, or by jobbers.

At the same time, basic service station economics also have impacted the conventional type outlet. The cost of running a conventional station has increased substantially. Payroll, equipment, utilities, taxes, and service expenses have soared. For example, the minimum wage has increased by 168% since 1966. Low volume outlets cannot cover costs. The breakeven volume on new stations has increased by five times or more since the sixties. The profits on gasoline are held down by the efficient competitors who respond to price-conscious customers through low cost marketing methods. Direct expenses of 2-5¢/gallon have been common for efficient gasoline-only stations, while full-facility outlets have been frequently running two to three times the cost per gallon to operate. The combination of market segmentation and basic economics have impacted on the population of conventional type stations, resulting in a large number of station closings.

The national trends in petroleum marketing have touched Sohio and the markets in which it operates with equal force. These trends, plus the unique divestiture requirements associated with the Sohio/BP merger, explain Sohio's overall decline in number of stations.

Congress, under Title III of the Petroleum Marketing Practices Act, required the Office of Competition of the Department of Energy to assess the pricing practices of the petroleum marketers. Their study, published in 1981, concludes that the decline in the proportion of sales through dealer outlets was the result of changes in consumer preference, not predatory pricing at or subsidization of company-operated stations. Rather, company-operated stations were operating profitably. The report shows that dealers supplied directly by refiners dropped in share of volume 14 percentage points from 1972 to 1979. The classes of trade which gained at the expense of the dealers were the branded jobbers and unbranded independents who together increased share by 13 percentage points. If it is the intent of Congress to insulate service station dealers from competition, then S.B. 40 is misdirected. It does not strike at these two groups that have been growing rapidly in share of market. In contrast, company-operated retail outlets showed an increase of only four percentage points during the period studied.

Sohio's operations, both in Ohio and on the East Coast, are consistent with these findings. The company is not engaged in predatory pricing nor subsidization in its company-operated network. Sohio's pricing philosophy concerning predatory pricing was expressed very clearly in 1947 by a company executive who had participated in pricing decisions since the 1920s. This philosophy was quoted by Dr. Edmund P. Learned of Harvard University in his book Gasoline Pricing in Ohio:

One of the fallacies often advanced is that so-called leading marketers reduce prices to drive out competition so that they may later enjoy a monopoly. That is like trying to sweep back the ocean to get a dry place to sit down. Competition is impelled by impersonal forces that never scare and never hesitate for a long time, and would move in immediately when prices were restored, offering little opportunity to a single marketer to recoup his losses. As a practical matter, selling below cost to drive out a competitor is a sure road to bankruptcy.

... The marketplace in a competitive economy provides a continuous customer plebiscite in which success depends entirely upon the ability of the marketer to please a customer at a profit.

It is, of course, appropriate to note that until the North Slope Alaskan crude oil, in which Sohio has a significant interest, began to flow in 1977, Sohio was essentially a refiner/marketer. At its previous peak of self-sufficiency in 1960, Sohio's own crude oil provided only 28.7% of crude oil processed at its refineries. Self-sufficiency in crude oil ranged between only 10 and 16% during the 1969-1976 period. Over a long history of 65 years, Sohio had become a highly efficient refiner/marketer. With this philosophy and expertise well developed, there was certainly no need to begin to engage in predatory pricing practices once

the company became fully self-sufficient in crude oil supplies in the 1977-78 period.

If company-operated stations are eliminated, motorists purchasing from these stations will immediately pay higher prices for gasoline. A number of surveys have shown that over time, leased dealer stations have been selling gasoline at about 3¢ a gallon above company-operated outlets.

The most comprehensive study on the impact of divorcement on gasoline prices in Maryland was completed in January, 1983 by Professors John R. Umbeck and John M. Barron of Purdue University. This is an update of their original January, 1982 study. The additional data give further support to the conclusions that Maryland divorcement reduced competition among gasoline retailers, raised retail prices, and did not benefit consumers. This was an exhaustive investigation of Maryland service stations before and after divorcement. The updated figures show that the average price of gasoline increased 3.5¢ per gallon at divorced stations and 1.5¢ per gallon at competitive non-divorced outlets. If this same economic impact occurred throughout the nation upon enactment of divorcement legislation, the authors estimate that motorists would pay \$1 billion more per year for their gasoline.

When company-operated stations were being eliminated in Maryland, there was an immediate push by the Dealer Association for dealers to raise prices. This prompted the Chief of the Antitrust Division of the Maryland Attorney General's office to write the Association, warning them of possible antitrust liability. To quote from that letter, "Because your members are competing businessmen, your recommendation raises serious antitrust concerns. We interpret your recommendation as an invitation to your members to raise their prices to non-competitive levels."

The proposed legislation would also reduce the availability of gasoline to motorists during evening and weekend hours, and particularly in times of gasoline shortages. Traditionally, company-operated stations have been open longer hours to serve the public than dealer-operated stations. A comprehensive study of hours of operation conducted in Ohio during May, 1983 showed that dealers average 101 hours per week as compared to 122 hours for company-operated stations. Thus, dealers are open three hours less per day. Further, 23% of dealers were closed on Sundays while less than 2% of company-operated outlets were closed on that day.

In the tight supply period of 1979, Sohio staggered the hours and days of operation at company stations so that many were open on weekends and in the evenings when motorists needed gasoline and when most dealers of all brands were closed. Further, extraordinary steps were taken to ensure that stations were open along Ohio interstate highways on summer weekends and during holiday periods, again when many dealer stations were closed. This accommodation would not be possible again if company-operated stations were prohibited.

Not only will retail divorcement cost the consumer money, freedom of choice, and convenience, it will jeopardize the livelihood and cause serious job dislocation for tens of thousands of company station employees throughout the U.S. All company station employees -- managers, assistant managers, mechanics, bookkeepers, cashiers, island salespersons -- will have to find new employers, needlessly disrupting income continuity and benefits. While many of the positions would still be in existence if stations were converted to dealer operation, it is highly probable that the new dealers would select employees other than those presently at the stations.

Also, very few employees want to become dealers in the current declining market. If this were their preference, they would be dealers today. Further, very few have the \$30,000 to \$50,000 investment required to become a dealer, or would want to go into debt to that extent in these very uncertain times. Our experience has shown that in most cases the fine, loyal employees who are successful in working as managers of our stations are not the same people who succeed as individual entrepreneurs.

Sohio/BP alone has approximately 11,000 full and part-time company station employees whose livelihood would be impacted by this legislation. Since Sohio has operated company stations for over half a century, many of these employees who would lose their jobs, managers and others, have been with Sohio/BP for over 25 years. In addition, hundreds of other accounting and clerical employees associated with the administration of company-operated stations would be adversely affected. This would be a stressful experience and would be taking place at a time when unemployment is still high and jobs are difficult to obtain.

In addition to the damage to competition which would be caused by the main thrust of S. 40 to prohibit refiner-operated stations, the open supply provisions of the bill would hurt, in the long run, the lessee dealers whom the bill is seeking to protect. Open supply, as proposed in S. 40 would cause severe consumer confusion, unfair competition, and lead to the demise of branded service station marketing, to the detriment of lessee dealers.

The brand of gasoline is still very important to a large segment of the motoring public. Over the years customers have come to rely on the brand to signify an expected level of product quality, service and other benefits, such as credit card acceptance. This consumer brand loyalty did not develop by chance; it was the result of planned investments in first-class service stations at high traffic locations, refinery units, product development, quality control and significant working capital.

Loyalty toward a brand of gasoline is very similar to the loyalty toward any consumer product, such as Maxwell House coffee or Tide laundry detergent. Customers of these brands have developed an expectation of quality and do not expect any surprises when they open a can of coffee, a box of detergent, or visit a service station. Although open supply would require the station dispensers to be appropriately marked, motorists would still be attracted to the station by the brand identification on the station building and on the I.D. signs. Having been drawn into the station, the customer would feel deceived by the offering of a product of another brand or no brand at all. His/her confidence in that station and others carrying the same brand would be severely shaken.

Open supply would allow a competitor to take unfair advantage of an established company's trademark/brand loyalty. A competitor could dump product into a station and draw upon the goodwill and investments of the original brand. In total, this provision could reduce the value of a major brand franchise and lead to a reduction of investment by major oil companies in branded lessee dealer type facilities.

The proposed legislation is also bad precedent. There is nothing unique about the petroleum industry in reaching the consumer through both company-operated and franchise-operated (dealer) retail outlets. This dual distribution system of marketing is commonplace in American commerce. It has enabled hundreds of thousands of small business people to successfully establish their own firms by capitalizing on the names and images of their suppliers.

Good examples of the degree to which firms in product/service areas other than petroleum market through both franchise and company-operated stores can be found in the lodging, fast food, convenience store, and electronics industries. In lodging, the Holiday Inn has some 14% of its inns, including 19% of its rooms, under a company-operated mode. McDonald's, the top fast food chain, has 26% of its units being operated by company personnel. Further, some 55% of its outlets are owned by the firm. In the convenience food store industry, 7-Eleven has over 60% of its units company-operated; and in the electronics field, Radio Shack also has over 60% of its retail stores operated by company personnel.

In each instance, the proportion of company-operated retail outlets of these firms exceeds that in the oil industry in the U.S. In addition, such well known manufacturers as Hart, Schaffner & Marx, Sherwin-Williams, and Firestone have 350, 1,410, and 1,300 company-operated outlets, respectively. Legislation to prohibit company-operated service stations would be outright discrimination against one industry.

Petroleum regulations were lifted three years ago. Since that time the price of gasoline has dropped by over 20¢ per gallon, excluding increases in taxes. Legislation such as S. 40 runs counter to the move to lift government controls from the marketplace and allow the consumer to benefit from competition in a free market. It would be unfair to American consumers to pass this legislation and have them find out by actual experience that gasoline prices increased when company-operated service stations were eliminated. Motorists need both company employee-operated stations and dealer-operated stations to ensure maximum competition in prices, hours of operation and services. We urge you to totally reject the concept of gasoline retail divorcement as embodied in S. 40.